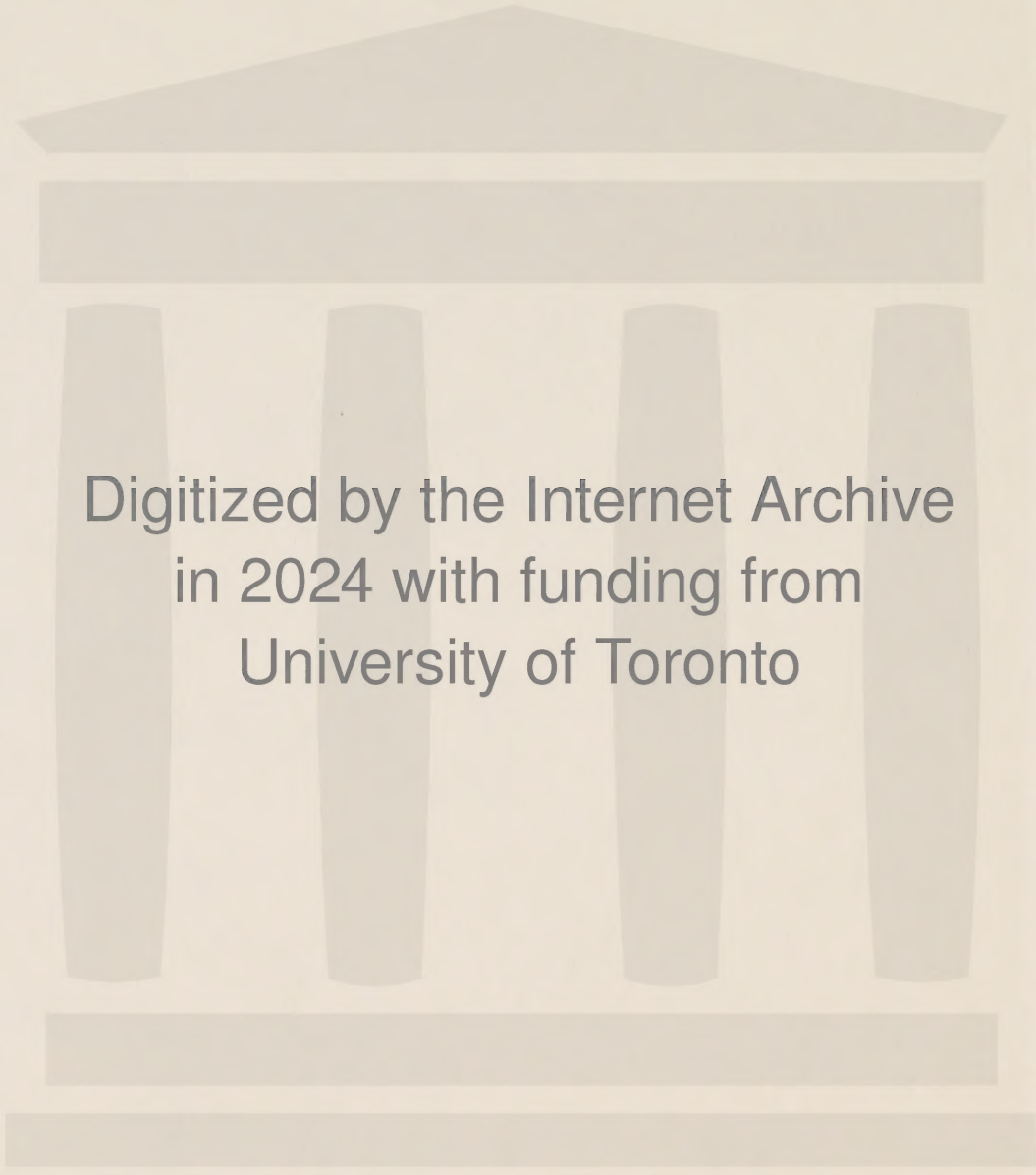

THE MINISTER'S ADVISORY COMMITTEE ON THE
IMPLEMENTATION OF THE LAND TRANSFER TAX ACT,
1974 AND THE LAND SPECULATION TAX ACT, 1974

c/o 51st Floor,
Toronto-Dominion Centre,
Toronto, Ontario,
M5K 1G1.

July 26, 1974

The Honourable Arthur K. Meen,
Minister of Revenue,
Parliament Buildings,
Queen's Park,
TORONTO, Ontario,
M7A 1X8.

Dear Mr. Meen:

THE LAND TRANSFER TAX ACT, 1974
THE LAND SPECULATION TAX ACT, 1974

On May 31, 1974, the Minister's Advisory Committee on the implementation of the above-mentioned Acts was provided Terms of Reference to:

(a) review general submissions made to the Ministry on the Acts;

(b) recommend to the Minister the solicitation of additional submissions of a general nature in respect of any aspect of the administrative procedures or regulations required to implement the Acts;

(c) make recommendations to the Minister in respect of any administrative procedures or regulations required to implement the Acts; and

(d) review the technical provisions of the Acts with a view to identifying and advising the Minister of any anomalies or provisions requiring clarification.

Our Committee met in plenary meetings on eleven days between the end of May and today. In addition, the two sub-committees which were formed to deal with each of the Acts met on several other days during the same period. Certain members of the Committee met with representatives of the legal profession specializing in real estate matters. Representatives of the Ministry of Housing, the Ministry of Tourism, and of the Law Property Branch of the Ministry of Consumer and Commercial Affairs attended our meetings. As you know, several officials of the Ministry of Revenue, including R. J. Weiers, Isaac Stephenson, W. Duggan and Gordon Jacobs acted as ex-officio members of our Committee. Mr. Duncan Allan of the Ministry of Treasury, Economics and Intergovernmental Affairs was also present at a number of our meetings.

The following are the highlights of our report.

LAND TRANSFER TAX ACT, 1974

We have recommended that a non-resident person who would otherwise be subject to the higher rate of land transfer tax (20%) should be subject to the lower rate of land transfer tax in respect of a conveyance under which he is acquiring a property for actual use and occupation by him for the purpose of conducting a commercial or industrial business carried on by him in Ontario.

The Honourable John White made two statements in his Budget Speech of April 9, 1974 that are particularly relevant to this recommendation. He said first that "In examining the problem of rapidly rising prices for real property in Ontario, it has become increasingly apparent that large scale acquisition of land by non-residents of Canada is a significant factor". He also stated: "I emphasize ..... that it is not our intention to penalize industries which seek to locate or expand in this province, although we would encourage these established companies to broaden Canadian equity participation". Referring to the Land Speculation Tax Act, Mr. White said: "There is no doubt ..... speculation ..... by non-residents bids up (land) prices artificially, increases the cost of housing and generates unwarranted windfall gains".

From these statements and others that have been made by Ministers, it would appear that the primary policy objective of the two statutes as they relate to non-residents is to curb large scale acquisitions of land

by non-residents to be held by them on a speculative basis or as passive "investors" and that a secondary policy objective is to avoid penalizing bona fide users of property who are actually occupying and using the subject land to commence or expand business activities in Ontario.

Members of our Committee have expressed serious reservations about the administrative and political wisdom of seeking to graft onto land transfer tax legislation a complex and totally discretionary review procedure along the lines of that provided for in the Foreign Investment Review Act (Canada). They have also questioned, as a matter of practicability, the efficacy of of such a tax based solely on the value of transferred land, and then only on land transferred to non-residents, as a tool to achieve the Government's apparent goals of economic planning and land use.

One of the fundamental and most important principles of modern taxing legislation is that its application to individual taxpayers not be contingent upon the exercise of a discretionary power by administrative or political authority.

A review procedure of the type apparently contemplated by the Government would constitute a significant departure from this principle and, in the opinion of the Committee, a significant retrograde step in the area of tax legislation. This would be a particularly inappropriate development in Ontario which, with some considerable justification, can regard itself as a leader not only in Canada but also in the English-speaking world in the field of modern and enlightened legislation regarding the rights of persons vis-a-vis governmental authority.

In our meeting of May 31, 1974, the Executive Director of the Fiscal Policy Division of the Ministry of Treasury, Economics and Intergovernmental Affairs indicated that his Ministry would attempt to provide our Committee with a position paper on land transfer tax exemption criteria. While our Committee has not yet received these criteria for review and comment, we believe that it would be an almost impossible task to arrive at any appropriate land transfer tax exemption criteria such as geographic location, type of industry, size of business, kind of land, etc.

It is noted that the Land Transfer Tax Act provisions regarding seasonal properties and permanent residences may have adverse economic effects on certain areas of the Province such as Northern Ontario. As this type of

consideration relates to a policy decision of the Government, no recommendation concerning this possible problem is contained in this report.

To avoid possible abuse, we recommend that the Land Transfer Tax Act be amended to provide that the registration of any form of notice of unregistered conveyance is deemed to constitute registration of such conveyance. Under the existing provisions of the Act, registration of a notice, caution, etc. that gives notice of a conveyance which is itself unregistered, does not appear to give rise to the tax. In the case of a lease, registration of a notice of lease rather than the lease itself is quite common for reasons that have nothing to do with land transfer tax. Unless the Land Transfer Tax Act is amended as recommended, there will be an inducement to avoid the tax by the notice of lease route.

Although we have made certain limited recommendations regarding the definitions of non-resident person and non-resident corporation in the Land Transfer Tax Act, we believe that these provisions require further study and consideration by the Committee and by the Government. We doubt that those provisions adequately achieve, in concept, the basic policy objectives of the statute, as we understand them, in relation to non-resident ownership of land. Moreover, we believe they are technically deficient from the point of view of both Government and taxpayers.

LAND SPECULATION TAX ACT, 1974

In our report, we have recommended that Section 4 of the Land Speculation Tax Act be amended by deleting clauses (i) and (j), which exempt government purchase or expropriation transactions from a tax otherwise payable if the transaction were with a private party.

Our Committee feels strongly that the provision of the preferred tax treatment of land transactions with the Ontario Government inherent in Section 4 (i) and (j) has created a situation which may adversely affect the future of the housing and land development industry in Ontario. This exemption from tax on transactions with government provides a mechanism, when coupled with the Ontario Land Corporation, for a substantially increased role by government in land development and a severe tax disincentive for transactions with anyone other than government. Each and every land transaction with the Government of Ontario, which might otherwise attract the 50% land speculation tax, would be under a cloud of suspicion. Unless

our recommendation of deleting clauses (i) and (j) of Section 4 is accepted, there would be created a potential two-price system for all Ontario land. On the grounds of horizontal equity from a tax policy viewpoint, these exemptions for government purchase or expropriation transactions should be repealed. In the situation where an owner of land is subject to expropriation, we have suggested that alternative relief should be provided in the form of a potential rollover, which would put that owner in the same position after the transaction as he was before, rather than in a better position as now provided under the existing provisions of the Land Speculation Tax Act.

We consider our recommendation with respect to Section 21 of the Land Speculation Tax Act to be of extreme importance. On pages 62 to 64 of our report, there are detailed recommendations, and reasons therefor, with respect to this provision dealing with subdividers. Our Committee is of the opinion that before a land development or subdivision transaction should be exempt from tax, there should be a significant addition of economic value to the designated land. If, however, this is achieved, we recommend a much broader exemption for the subdivider who sells serviced land.

There are a number of extremely complex areas in both Acts, where we have not yet provided firm recommendations, which require further substantial study by the Government. In lieu thereof, we have endeavoured to define the problems by setting out observations, suggestions and a study paper for each topic:

* the problem area of deemed dispositions on change in share control of a corporation and the possible adverse effect on the minority shareholder;

* the implementation of a number of rollover provisions, i.e. tax-free transfers, which we have recommended in the case of the transfer of designated land between spouses, members of the family, parent-subsidiary relationships, etc.

* the liability for tax on the initial entering into of a lease, which in our view, should be an exempt transaction for the purposes of the Land Speculation Tax Act.

We urge you to implement our Committee's recommendations as soon as possible in the form of regulations; however, a number of our recommendations cannot remain as regulations but, instead, should be enacted as amendments to these statutes during the fall session of the Legislature. We further suggest that as soon as possible public announcement be made as to how the Land Speculation Tax Act will be interpreted in the areas of subdividers' sales of land to builders, tax-free rollovers, and a number of our recommendations pertaining to farmers. In addition, we would hope that you would announce the prospective repeal of Sections 4(i) and (j) of the Land Speculation Tax Act.

The Committee has provided you with comments on the deductibility of the land speculation tax for income and corporation tax purposes, and we hope that this matter will be resolved between the Province of Ontario and the Federal Government with all due dispatch.

We have previously advised you of our recommendation that a number of the technical regulations which will be drafted as a result of our recommendations should be reviewed in advance by our Committee and members of the legal profession specializing in real estate matters.

This interim report is the submission of the entire Advisory Committee. We feel that it is in the public interest that information on possible changes in these two Acts be made available to the private sector. For this purpose, we recommend that this report be made available to the public in whatever manner you consider appropriate.

Unquestionably, there are recommendations in which some of us would wish for a different emphasis in expression, or a different reason expressed for a recommended change, but after substantial discussion on these complex, and somewhat novel pieces of legislation, we are now willing and satisfied to join in subscribing our names to the report which follows.

The members of the Advisory Committee wish to thank you, as Minister of Revenue, and the Government of Ontario for this opportunity of serving our Province.

We would be pleased to meet again in September or to provide any other assistance which may be required by your Ministry.

Respectfully submitted,

R. M. Anson-Cartwright, F.C.A., Chairman

R. P. Simon

Arnold Englander

Lawrence Shankman

Alan D. Laing, C.A.

John A. Tuck

John D. Richardson, C.A.

E. M. McIlwee

Michael Davies

William Allan

W. Mitchell

Ross Reilly

J. C. Phillips, Q.C.

J. R. O'Kell, Q.C.

Alternate Members

Don Wyekoff
(alternate for W. Mitchell)

G. E. Bell
(alternate for J. C. Phillips)

Douglas Andison
(alternate for J. R. O'Kell)

D. N. Morris, C.A.
(alternate for L. Shankman)

cc: The Honourable Wm. G. Davis
The Honourable John White
Mr. D. A. Crosbie

The Land Transfer Tax Act, 1974

SUGGESTED AMENDMENTS

RECOMMENDATIONS FOR AMENDMENTS TO THE LAND TRANSFER TAX ACT

Registration of Notice of a Conveyance:

1. RECOMMENDATION: That the LTTA be amended to provide that the registration of any form of notice of any unregistered "conveyance" (as defined in S. 1(1)(c)) shall be deemed to constitute registration of such conveyance, and that provision be made to permit deferral of payment of the tax, if any, arising in respect thereof until the earlier of

   (a) the time when the transaction that is effected by the conveyance is closed, and

   (b) the transferee under the conveyance goes into possession of his interest in the land

   if registration of the notice precedes such event.

COMMENT: Subsections 2(1) and 2(2) impose tax upon the tender for registration of "..... a conveyance whereby any land is conveyed ..... to any transferee". Registration of a notice, caution, caveat or similar document that gives notice of a "conveyance" which is itself unregistered does not appear to give rise to tax. Because registration of such a notice, caution, caveat etc. may provide substantial protection to an owner of an interest in land, thus making registration of the actual conveyance less significant to him, there will, unless the Act is amended as recommended, be an inducement to avoid the tax in this way. (In the case of leases registration of a notice of lease rather than the lease itself is quite common for reasons that have nothing to do with land transfer tax.) If the Act is amended as suggested, registration of taxable notices, caveats etc. (other than notices of lease) will be infrequent and consequently provision of a mechanism to permit deferral of any tax payable, as recommended, should not cause significant administrative problems.

Assignment of Mortgages:

2. RECOMMENDATION: That the definition of "land" in S. 1 (1)(d) of the LTTA be amended by adding at the end thereof the words "but 'land' does not include an interest held in land solely as security for some indebtedness secured by the land". (See Land Speculation Tax Act ("LSTA"), S. 1(1)(b)).

COMMENT: Although transfers of land made to secure or discharge a mortgage are not subject to tax (S. 1(1)(b)), assignments of existing mortgages appear to be taxable when registered. This was not the case under the old Land Transfer Tax Act and such assignments are specifically excluded from the definition of "designated land" under the LSTA (S. 1(1)(b)). The subjection of transfers of such security interests to tax under the LTTA appears to be a drafting oversight. The wording suggested for the amendment is taken without change from the LSTA.

Resident status of a "Public Corporation":

3. RECOMMENDATION: That

1. The LTTA be amended by adding paragraph 1(1)(fa) immediately after paragraph 1(1)(f) thereof that a corporation that is, at the time at which the determination of its resident status under the Act is being made, a "public corporation" within the meaning of the Income Tax Act (Canada), may establish in prescribed manner that the circumstances of share ownership described in subparagraphs 1(1)(f)(i) and (ii) do not apply to it.

2. Regulations be prescribed under such provision that adopt an approach similar to that used in Regulation 3100 of the Income Tax Regulations (Canada), but applicable to all "public corporations" (as described above); and

3. That a regulation be prescribed to provide that, unless more than 10% of the shares of any "public corporation" (as described above) are owned by any one non-resident person, or any group of non-resident persons who act in concert in relation to the corporation, paragraph 1(1)(f)(i) does not apply for purposes of determining the resident status of such corporation.

COMMENT: In the absence of some rules and procedures such as those recommended it will be impossible for many corporations whose shares are widely held to establish definitively their resident status for purposes of either the LTTA or the LSTA. And in cases where such a corporation is at or near the dividing line, its status can fluctuate from day to day. A definitive set of rules and compliance procedures is required and there would appear to be little if any opportunity for significant abuse under the approach recommended. With regard to clause 3 above, see submission of Purdy Crawford of Osler, Hoskin & Harcourt attached as Exhibit 1. With regard to all three recommendations, see outline of suggested regulations attached as Exhibit 2.

Exhibit 1

OSLER, HOSKIN & HARCOURT
BARRISTERS & SOLICITORS

AREA CODE 416 TELEPHONE 362 2111
CABLE ADDRESS "CARTHOS"
TELEX 06 22457

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EDWARD SAUNDERS, Q.C.
PURDY CRAWFORD, Q.C.
D. F. PATTISON
BERTHA WILSON, Q.C.
J. R. MOFFAT
F. A. M. TREMAYNE
S. R. ELLIS
D. E. WAKEFIELD
J. M. ROLAND
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R. G. FERGUSON, Q.C. J. G. OSLER, Q.C.

THE PRUDENTIAL BUILDING
4 KING STREET WEST
TORONTO, CANADA
M5H 1B9

July 11, 1974.

Ronald M. Anson-Cartwright, Esq.,
Chairman,
Ad Hoc Advisory Committee on Land Speculation
Tax Act and Land Transfer Tax Act,
Price, Waterhouse & Co.,
P. O. Box 51,
Toronto-Dominion Centre,
Toronto, Ontario.

Dear Sir:

Re: Land Transfer Tax Act

There are one or two aspects of the definition of "non-resident corporation" in this Act which have caused us and certain of our clients some concern.

To set the problem in context it relates to the application of the definition to a corporation which may be clearly under de facto Canadian control either because a large block of shares is owned by a Canadian resident or a group of Canadian residents or because the shares of the corporation are so widely held that the company is controlled by its management which is based in Canada. The corporation may not be able to establish however that it is not a non-resident corporation within the meaning of Section 1(1)(f)(i) of the Act because of its inability to ascertain whether all its registered shareholders actually own the shares registered in their names or whether such shares are held in trust for persons who may or may not be residents of Canada. Further the corporation may actually have a recorded share ownership that indicates 50% or more of the votes are represented by shares registered in the name of a substantial number of widely scattered non-residents who do not individually own any substantial block of shares.

This can result in what is obviously a Canadian controlled company being classified as a non-resident corporation under the Act and we suggest that the Act should be amended or a regulation enacted to change this result.

Ronald M. Anson-Cartwright, Esq. July 11, 1974.

We have given some thought as to how this matter might be dealt with by a regulation which would exempt such a corporation on the basis of a determination that the Act was not intended to apply to such a corporation and at the same time not create any loopholes which would result in the Act not being applicable in circumstances where it was obviously intended to apply. One approach that might be taken is one which would be consistent with the amendment to Section 1(1)(f)(ii) which was made to the Act during the course of its enactment whereby even if any one non-resident person owns shares representing 25% or more of the vote, it can still avoid being classified as a non-resident person on the basis therein outlined. Under this approach if the aggregate number of shares owned by a non-resident or by a group of non-residents is not in excess of a specified amount and the corporation is in fact controlled in Canada, it would not be regarded as a non-resident person. To illustrate our suggested approach in specific terms we have prepared and enclose two alternative outlines of the wording which might be used in a regulation. If the first alternative approach is taken then because of the limitation on the number of shares that can be held by a non-resident person or group of non-resident persons we do not think ministerial discretion would be required. On the other hand if alternative number 2 were considered (which would be more consistent with Section 1(1)(f)(ii) then ministerial discretion would probably be required. We prefer alternative number 1 since, as lawyers, we like to avoid the use of ministerial discretion.

I would be glad to discuss this matter further if you so desire.

Yours very truly,

Purdy Crawford

HPC:kg
cc. The Honourable Arthur Meen
The Honourable John White
DELIVER

Alternative 1

Outline of suggested regulation re Section 1(1)(f)(i) of the Act

Subclause 1(1)(f)(i) of the Act does not apply where (i) no non-resident person or no group of non-resident persons owns shares of the corporation to which are attached 10% or more of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, and (ii) the corporation is not in fact controlled, directly or indirectly, by a non-resident person or group of non-resident persons.

Any references in the Act to a "group of non-resident persons" does not include an aggregation of persons or any part thereof who together own all of or any part of the shares of, or all of the shares or any part of the shares of a particular class of, any corporation in relation to which the reference is relevant, except where those persons act in concert with one another in any matter or transaction affecting the corporation or its management, ownership or financial affairs.

Alternative 2

Outline of suggested regulation re Section 1(1)(f)(i) of the Act

Subclause 1(1)(f)(i) of the Act does not apply where it is established to the satisfaction of the Minister (i) that no non-resident person or no group of non-resident persons owns shares of the corporation to which are attached 25% or more of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, and (ii) that the corporation is not in fact controlled, directly or indirectly, by a non-resident person or group of non-resident persons.

Any references in the Act to a "group of non-resident persons" does not include an aggregation of persons or any part thereof who together own all or any part of the shares of, or all of the shares or any part of the shares of a particular class of, any corporation in relation to which the reference is relevant, except where those persons act in concert with one another in any matter or transaction affecting the corporation or its management, ownership or financial affairs.

Exhibit 2

OUTLINE OF SUGGESTED REGULATION RE PARAGRAPH 1(1)(f) OF THE LAND TRANSFER TAX ACT

1. In the case of a corporation that is, at any time at which the provisions of paragraph 1(1)(f) of the Act are being applied in respect thereof, a "public corporation" within the meaning of paragraph 89(1)(g) of the Income Tax Act (Canada), for purposes of paragraph 1(1)(f) of the Act the following rules apply:

   (1) subparagraph 1(1)(f)(i) of the Act does not apply unless one non-resident person or a group of non-resident persons owns shares of the corporation to which are attached 10% or more of the voting rights ordinarily exercisable at meetings of the shareholders;

   (2) for the purposes of subparagraph 1(1)(f)(v) of the Act a corporation shall be deemed not to be controlled directly or indirectly by more than one non-resident person unless it is in fact controlled, directly or indirectly, by a group of non-resident persons; and

   (3) for the purposes of subsections (1) and (2) the term "group of non-resident persons" does not include any aggregation of persons unless the persons comprising such aggregation act, directly or indirectly, in concert with one another in matters or transactions affecting the ownership, management or financial affairs of the corporation in respect of which the expression is relevant.

2. (1) Where at any time in the 120-day period immediately preceding the time in respect of which the determination of the non-resident status of a corporation is relevant for the purposes of the Act or of the Land Speculation Tax Act, 1974, an authorized officer of a corporation, by knowledge of the name and resident status of a sufficient number of shareholders of the corporation is satisfied that subparagraph 1(1)(f)(i) or (ii) of the Act does not apply, whether by operation of subsection 1(1) or otherwise, he may so establish on behalf of the corporation by completing and filing with the Minister a prescribed form.

(2) Where, at any time in the 120-day period described in subsection (1) in respect of a corporation,

(a) the corporation was a public corporation within the meaning of paragraph 89(1)(g) of the Income Tax Act (Canada), and

(b) circumstantial evidence indicates that it is not reasonable to conclude that subparagraph 1(1)(f)(i) or (ii) of the Act applies, whether by operation of of subsection 1(1) or otherwise, to make the corporation a non-resident person,

an authorized officer of the corporation may establish on behalf of such corporations that such subparagraph does not apply by making and filing with the Minister a sworn declaration setting forth the facts upon which he relies in concluding that paragraphs (a) and (b) are applicable in respect of such corporations.

Resident Status of a "Mutual Fund Trust":

4. RECOMMENDATION: That, for purposes of determining the resident status, for purposes of the LTTA, of a trust that is a "mutual fund trust" within the meaning of the Income Tax Act (Canada), a procedure analagous to that of Recommendation 3 for public corporations be implemented.

COMMENT: Mutual fund trusts are, by definition under the Income Tax Act, widely held investment vehicles and the problem they face in determining definitively their resident status under the LTTA is similar to that experienced by public corporations.

"Non-Resident Persons" - Individuals:

5. RECOMMENDATION: That S. 1(3)(a) be repealed.

COMMENT: At present the combined effect of S. 1(1)(g)(i) and 1(3)(a) is to confer automatic and irrebutable resident status on a "landed immigrant" (i.e. one " ..... who has been lawfully admitted to Canada for permanent residence in Canada .....") from the day of his arrival in Canada, regardless of whether he can reasonably be said to be "ordinarily resident" in Canada in the usual sense of that term. This can lead to abuse. It is both appropriate and reasonable to put such a person on the same basis as a Canadian citizen - i.e. that he must establish that he is "ordinarily resident" in Canada in addition to holding the requisite immigration status. (Consideration might also be given to restricting S. 1(3)(b) so that it applies only to Canadian citizens.)

"Non-Resident Person" - Trusts:

6. RECOMMENDATION: That the words "established by a non-resident person within the meaning of subclause (i), (ii) or iv or" in the first three lines of S. 1(1)(g)(iii) be deleted from the LTTA.

COMMENT: It should be immaterial that the person who originally "established" the trust was, at the time, a "non-resident person". So long as the requisite percentage of beneficial ownership is, at the time at which the determination is relevant, owned by resident persons the policy objective of the statute is satisfied. There are, for instance, a large number of pension fund trusts and profit sharing plan trusts that were originally "established" by Canadian subsidiaries of non-resident parent corporations but whose funds and assets are now held entirely for the benefit of Canadian resident employees. There are also real estate investment trusts (REIT's) which were established by non-resident persons but the majority of the trustees are resident Canadian citizens not affiliated with the non-resident who established the trust and all or virtually all the beneficiaries under the trusts, the unit holders, are Canadians. It cannot be intended that such trusts be fixed forever with "non-resident" status.

"Non-Resident Person" - Unit trusts:

7. RECOMMENDATION: That Section 2 (2) of the LSTA be amended to include provisions analogous to subclauses (vi) and (vii) of Section 1 (1)(d) of the LSTA to cover trusts and beneficial interests in trusts.

COMMENT: The beneficial ownership of land held in a trust, for example a unit trust, can be transferred by way of a transfer of the units or similar beneficial interests in the trust. There appears to be a loophole in the scheme of the two Acts (LTTA and LSTA) combined in their attempt to encompass, at least, transfers of the beneficial ownership of "designated land" where control of the designated land passes to non-residents. This occurs because transfers of trust interests are not caught by the LTTA and the charging provisions of S. 2(2) of the LSTA refer only to dispositions described in subclauses (vi) and (vii) of S. 1(1)(d) of that Act. Those subclauses encompass only transactions involving corporations and their shareholders.

S.2 - Charging Provisions:

8. RECOMMENDATION: That the words "or in trust for" be deleted from the second and third lines of each of subsections 2(1) and 2(2) of the LTTA.

COMMENT: For purposes of the Act a trust is an entity or person, the trustee of such trust is himself a transferee and a conveyance to a trustee is taxable under either 2(1) or 2(2), depending upon the resident status of the trust itself as determined under S. 1(1)(g). The language of these two subsections referred to in the recommendation is confusing in that it seems to suggest that, in some instances at least, the status of a trust as a separate entity should be ignored. This may lead to unintended problems of interpretation - e.g. where a trustee takes a conveyance in trust for A (40%), a non-resident person and B (60%), a resident person. (The recommendation and comments are equally applicable to the use of the same words in S. 4(3)(a)).

Land Acquired by Non-Resident Person for Development:

9. RECOMMENDATION: That S. 16(1) of the LTTA be repealed and replaced with provisions that give effect to the following scheme to apply to non-resident persons who are land developers:

   1. Provided that either

      (a) the non-resident person holds a valid Registration Certificate (which could be made subject to renewal annually or at some other appropriate interval) issued by the Minister, or

      (b) the land in question is processed and resold in accordance with conditions, including any time limits as to resale, agreed to in writing between the Minister and the non-resident person

      the amount of the difference between the tax under S. 2(2) and 2(1) would be deferred and become payable only if, at a time when the subject land was still owned by the non-resident,

      (c) in any case referred to in (a), he ceased to hold a valid Registration Certificate, or

      (d) in any case referred to in (b), he failed to comply with the conditions agreed to in writing with the Minister

      and the Minister would be authorized to accept, as security for the tax thus deferred, any security satisfactory to him (in lieu of providing in the Act that the whole of the subject property automatically becomes subject to a lien for the deferred tax).

   2. If the subject land is sold by the non-resident person before the happening of the event referred to in 1(c) or 1(d), as the case may be, the deferred tax would be cancelled, as presently contemplated by S.16(3) of the Act.

   3. There should be no requirement that the non-resident person, at the time of his purchase of the subject land, satisfy the Minister as to the resident status of ultimate purchasers of the land from him.

COMMENT: The recommendation contemplates (and the Act, or Regulations made pursuant to a specific provision in the proposed amendment, should so provide) that a Certificate of Registration would be issued only to a non-resident person who satisfies the Minister that his principal business in Canada includes, as a significant component thereof, the active subdivision, servicing and sale of real property. The desired policy objective of the Act would appear to be achieved - and in fact fostered - by facilitating and encouraging the active development of land by such persons. In cases where the non-resident person does not hold a Registration Certificate, the policy objective can be achieved by the imposition by the Minister of conditions which he considers to be appropriate in the circumstances. In either case if land is actually being developed and resold the results desired by the Government are presumably being achieved and, as a policy matter, the tax otherwise payable under S. 2(2) should be foregone.

This should be so regardless of the resident status of any subsequent purchaser of the land. If the development function is being satisfactorily performed by the "non-resident" developer, there is no logical reason to impose a S. 2(2) tax on him because the person buying from him is a "non-resident person". (Think of the housing development with 250 single family units of which 5 are eventually sold to non-resident persons - who will be required to pay S. 2(2) tax on their purchase price).

The ability to provide security to the Minister otherwise than by way of a statutory lien imposed on the whole of the subject land will give the taxpayer much more flexibility and may substantially simplify his financing arrangements. The Minister will be fully protected since he must be satisfied as to the adequacy of the security offered.

The Registration Certificate procedure will greatly simplify and expedite both compliance by taxpayers and administration by government officials in respect of bona fide and active development activities being carried on in Ontario by developers who are "non-resident persons" within the meaning of the Act. And a requirement for periodic renewal of the registration certificates will permit the Government to guard against abuse. It must be presumed that the Government favours active and effective competition in the land development industry as one means of ensuring competitive pricing of serviced lots.

This objective will be fostered by facilitating to the greatest extent possible, consistent with the policy objectives of the LTTA, the continued participation by bona fide, active land developers in the land development industry in Ontario notwithstanding that they are "non-resident persons" for purposes of the Act.

Non-Resident Persons: Final Orders of Foreclosure:

10. RECOMMENDATION: That S. 16(4) of the LTTA be repealed and reenacted to provide that where it is established that, in the case of a tender for registration of a final order of foreclosure that would otherwise be taxed under S. 2(2), it is established that

    (a) the mortgagor and mortgagee were dealing at arm's length,

    (b) the foreclosure was effected for the purpose of safeguarding the rights or interests of the mortgagee in respect of a loan made by him, the whole or any part of which is outstanding, and

    (c) neither the giving of the mortgage nor the foreclosure in respect thereof was carried out for the purpose of avoiding payment of tax under S. 2(2) of the Act.

    tax shall be payable under S. 2(1) in respect of such final order.

COMMENT: There is evidence that the potential tax under S. 2(2) on foreclosures will inhibit the flow of mortgage funds into Ontario from non-resident lenders simply because, as between two otherwise equal risk situations in Canada, this is an added risk element attaching to an Ontario mortgage. In fact there will be very few cases where this will become relevant and even fewer cases where the foreign borrower will not dispose of the foreclosed property at the earliest opportunity consistent with appropriate market and other relevant conditions. There can be no significant risk to the Government's policy objectives in the adoption of the recommended provision. If evidence of abuse manifests itself in the future (which seems most unlikely) remedial amendments can be made at that time.

"Non-Resident Corporation" - Definition:

11. RECOMMENDATION: That S. 1(1)(f)(i) of the LTTA be amended by adding after the words " ..... or by one or more corporations incorporated, formed or organized elsewhere than in Canada" the parenthetical phrase (other than any such corporation that is controlled directly or indirectly by one or more persons who are not non-resident persons) or by otherwise altering the definition of "non-resident corporation" to achieve the indicated result.

COMMENT: As S. 1(1)(f)(i) is presently worded a Canadian subsidiary of a foreign incorporated corporation that is itself controlled (e.g. wholly-owned) by a Canadian resident (e.g. an individual resident in Canada) is a "non-resident corporation". This is clearly an inappropriate result and cannot have been intended by the draftsman.

Non-Resident Insurance Corporations:

12. RECOMMENDATION: That, in the case of a corporation that is a "non-resident person" but

(a) is registered to carry on business in Canada under the Canadian and British Insurance Companies Act (Canada) or under the Foreign Insurance Companies Act (Canada),

(b) is licensed to carry on business in Ontario under the Insurance Act (Ontario), or

(c) is a corporation incorporated in Canada that is subsidiary to a corporation described in (a) or (b)

tax be payable under S. 2(1) and not under 2(2) of the LTTA in respect of transfers of land included in the assets such corporation is required to maintain to meet the legal requirements imposed on it in respect of investment of its assets in Canada.

COMMENT: See separate representations made by The Canadian Life Insurance Association.

RECOMMENDATIONS FOR REGULATIONS UNDER THE LAND TRANSFER TAX ACT

Exemption - Tax Otherwise Payable Not More Than $1.00

14. RECOMMENDATION: That all conveyances be exempted where the tax otherwise payable under S. 2 would be not more than $1.00.

COMMENT: A regulation to this effect would exempt all releases, quit claim deeds and similar "conveyances" where only nominal considerations are involved. (A similar administrative practice under the old Act was of doubtful legal validity.)

Exemption - Conveyances to Estate Beneficiaries

15. RECOMMENDATION: That any conveyance made to a transferee who takes the property in the capacity of a beneficiary, whether as a specific devise, as a distribution of the residue of an estate or on an intestacy - e.g. pursuant to the Devolution of Estates Act, be exempt from tax. The basic test for exemption should be whether the transferee is receiving the property in satisfaction of all or part of his beneficial interest in the estate of the deceased.

COMMENT: The rationale for such a rule is that the value of the consideration being given by the transferee is nil. It should not matter, for example, that the beneficiaries of an estate may, as between themselves and perhaps in agreement with the Executor, have agreed to an allocation amongst themselves of specific assets different from that provided for in the will. Although technical distinctions can be made in various circumstances that might support an argument for some tax, such lines are difficult to draw and the distinctions become fine. A general rule such as that proposed does not offend the policy of the Act, is more equitable as between beneficiaries in marginally different legal situations and will be far easier to administer.

Exemption - Conveyances Arising out of Marriage Relationships

16. RECOMMENDATION: That all conveyances made between spouses or ex-spouses pursuant to a marriage contract, a separation agreement or a settlement made in conjunction with divorce action be exempt.

COMMENT: It seems particularly inappropriate for the Government to impose a tax on a transaction made necessary by the break-up of a marriage. But in addition to this consideration, a difficult practical problem is that of determining the "value of the consideration" involved in such transactions. All these problems are overcome by the recommended rule at very little cost in revenue terms but at significant savings in terms of administrative and political headaches.

Section 2(2) Exemption - Non-Resident Persons: Principal Residences

17. RECOMMENDATION: That a person otherwise taxable under S. 2(2) of the LTTA who intends to become ordinarily resident in Canada within 6 months time be subject to tax at the rate prescribed in S. 2(1) of the Act in respect of a conveyance under which he is acquiring a property for actual use and occupation by him as his principal residence (which would not include recreational property).

COMMENT: Almost all persons who come to Ontario from a foreign jurisdiction and intend to stay long enough to justify, as a practical matter, purchase of a residence will soon acquire landed immigrant status. But there is often a delay. Immigration procedures take 8-10 weeks and perhaps as much as 4 months. It is now possible for many of such persons to obtain a temporary work permit pending issue of landed immigrant status. But, as the Act now stands and given the price of housing and the cost of a 20% tax on such price, such persons will be put to the unreasonable inconvenience of having to go into temporary accommodation until their landed immigrant status is received.

On the other hand few people who do not apply for landed immigrant status can stay here longer than 1 year on a work permit and very few, if any, of such persons would be interested in purchasing a residence. In view of these facts it seems unreasonable to continue the temporary road block that the Act now contains for a prospective landed immigrant. Nor is there any risk of significant instances of "passive" foreign ownership of Ontario property developing out of these circumstances.

Such a provision would also cover a Canadian citizen purchasing a principal residence prior to his return from abroad.

Section 2(2) Exemption - Employers who are Non-Resident Persons: Purchase of Property for Use as Principal Residence by Employees

18. RECOMMENDATION: That a person otherwise taxable under S. 2(2) be subject to tax at the rate prescribed in S. 2(1) in respect of a conveyance under which he is acquiring a property for actual use and occupation by one or more of his employees as his (their) principal residence.

COMMENT: This recommendation is a natural and reasonable extension of the recommendations 17 and 19.

Section 2(2) Exemption - Non-Resident Persons: Property Acquired for Business Use.

19. RECOMMENDATION: That a person otherwise taxable under S. 2(2) be subject to tax at the rate prescribed in S. 2(1) in respect of a conveyance under which he is acquiring a property for actual use and occupation by him for the purpose of conducting a commercial or industrial business carried on by him (including a property acquired by him to be leased by him, in the ordinary course of his business of selling goods or rendering services, under an agreement by which the lessee undertakes to use the property to carry on the business of selling, or promoting the sale of, such goods or services). (Such exemption should not extend to include land that is included in the inventory of a business carried on by the non-resident person.)

COMMENT: When he announced the new LTTA Mr. White, the Treasurer, made two statements that are particularly relevant to this recommendation. He said first that "In examining the problem of rapidly rising prices for real property in Ontario, it has become increasingly apparent that large scale acquisition of land by non-residents of Canada is a significant factor" (emphasis added). He also stated "I emphasize ..... that it is not our intention to penalize industries which seek to locate or expand in this province, although we would encourage these established companies to broaden Canadian equity participation" (emphasis added). Referring to the Land Speculation Tax Act Mr. White said "There is no doubt ..... speculation ..... by non-residents bids up (land) prices artificially, increases the cost of housing and generates unwarranted wind fall gains".

From these statements and others that have been made by Ministers it would appear that the primary policy objective of the two statutes as they relate to non-residents is to curb large scale acquisitions of land by non-residents to be held by them on a speculative basis or as passive "investors" and that a secondary policy objective is to avoid penalizing bona fide users of property who are actually occupying and using the subject land to commence or expand business activities in Ontario.

These policy objectives, if they are correctly discerned, would be well served if Recommendation 19 were implemented. Such a regulation would in no way undermine the efficacy of the LTTA as a deterrent to speculative acquisitions by non-residents or to the acquisition of substantial interest to be held by non-residents as passive investors. It would, on the other hand, have a number of significant advantages: it would give effect to the stated policy objective of not penalizing industries that locate or expand in Ontario: it would greatly simplify the operation and administration of the Act: in particular it would render unnecessary a great volume of administrative and political value judgments that have the potential for being extremely difficult and sensitive for the administration and for the Government.

Members of the Committee have expressed very serious, strongly felt reservations about the administrative and political wisdom of seeking to graft onto land transfer tax legislation a complex and totally discretionary review procedure along the lines of that provided for in the Foreign Investment Review Act (Canada). They have also questioned, as a matter of practicability, the efficacy of such a tax based solely on the value of transferred land - and then only on land transferred to non-residents - as a tool to achieve the Government's apparent goals of economic planning and land use.

If regulation by the Government for these purposes is justifiable, it should not be limited to land use by non-residents only but should apply to land use by all persons, resident and non-resident alike. A land transfer tax on non-resident purchasers is an inappropriate vehicle as a control mechanism for these purposes and, as a practical matter, would probably prove to be largely ineffective in achieving the apparently hoped for planning and land use results.

One of the fundamental and most important principles of modern taxing legislation as it has developed in Anglo-American jurisdictions is that its application to individual taxpayers not be contingent upon the exercise of a discretionary power by administrative or political authority.

A review procedure of the type apparently contemplated by the Government would constitute a significant departure from this principle and, in the opinion of the Committee, a significant retrograde step in the area of tax legislation. This would be a particularly inappropriate development in Ontario which, with some considerable justification, can regard itself as a leader not only in Canada but in the English speaking world in the field of modern and enlightened legislation regarding the rights of persons vis-a-vis governmental authority.

Section 2(2): Non-Resident Persons: Final Order of Foreclosure

20. RECOMMENDATION: That a person otherwise taxable under S. 2(2) be subject to tax at the rate of prescribed in S. 2(1) in respect of a conveyance that is a final order of foreclosure where the initial steps leading to foreclosure were taken by the mortgagee prior to April 10, 1974.

Exemption - "Rollover" Transactions with Related Corporations

21. RECOMMENDATION: That a conveyance be designated to be an exempt conveyance if it effects:

1. a transfer of land from a corporation to a shareholder thereof in the course of and pursuant to a liquidation, winding-up, or dissolution of the corporation;

2. a transfer of land between a person, other than a corporation, and a corporation if, immediately after the transfer, that person owned not less than 80% of the shares of each class of the outstanding shares of the corporation, or

3. a transfer of land between two controlled corporations

and, for purposes of this provision any two corporations are deemed to be "two controlled corporations" if immediately after the transfer

4. one owns not less than 80% of the shares of each class of outstanding shares of the other; or

5. not less than 80% of the shares of each class of shares outstanding of each of the two corporations are owned by a single third corporation.

COMMENT: In the definition of "conveyance" in S. 1(1)(b) of the LTTA the concept of transfer of legal ownership without any change of beneficial ownership is accepted as a non-taxable event. The same principle of exemption is logically appropriate in the case of inter-company transfers so long as there is a high degree of continuity of economic ownership. This becomes particularly important when the applicable rate of tax - e.g. 20% under S. 2(2) - becomes very significant in relation to the value of the asset being transferred. The rollover regime suggested by the recommendation requires a high degree of continuity of economic ownership, is limited to a relatively narrow group of transactions and would not expose the Act to undue avoidance. (There is a potential avoidance problem under S. 2(2) of the LSTA where designated land is held in a sub-subsidiary (third tier) corporation and shares of the parent (first tier) corporation are sold.

Although the proposed rollover regime might be said to potentially exacerbate this problem, the answer is that the problem itself must be solved and, when this is done, any ancilliary effect of the proposed rollover regime will also disappear. Departmental officials are aware of the S. 2(2) problem under the LSTA).

It has been suggested by officials that complete exemption of such transactions from tax, as opposed to tax at the low rate (S. 2(1)), may be unattractive to the Government. The reasons given were that tax was payable under the old Act on such transactions, has therefore become "institutionalized" and the Government will be "reluctant to forego the revenue". These reasons are difficult for the Committee to accept in the face of what, in its view, is a sound logical and reasonable case for full exemption. And, given the dramatic increase in revenue that the LTTA and LSTA will produce it would be particularly inappropriate to deny exemption on the basis of the relatively small revenue loss that would flow from such a provision.

Value of Consideration: Time of Determination

22. RECOMMENDATION: That where the consideration that is required to be valued under S. 2, and 1(1)(m) is something other than cash, the value thereof shall be deemed to be the fair market value thereof on the date when the agreement reflected in the conveyance was entered into by the parties (i.e. as opposed to the closing date or the date of tendering for registration of the conveyance).

COMMENT: The Act is, as presently worded, uncertain in its application to these situations. Certainty is desirable, since significant fluctuations in value of the consideration in question can occur, and the reasonable date for valuation would seem to be the date when the bargain was struck.

Value of consideration: Leases:

22. RECOMMENDATION: That, in the case of a lease that is a taxable conveyance, its value for purposes of S. 2 of the Act be as determined under 2. below, or, if an amount is determinable under 1. below, the lesser of

1. where the amounts and times of payment of rent under the lease are reasonably determinable, the present value of the lease payments (determined as if the lease payments were computed, or to be computed, on a net, net basis) determined on the basis of a discounting factor that reasonably reflects the then current market interest rates, and

2. the present fair market value of the leased property less a prescribed percentage thereof determined by reference to the length of the term of the lease, including options and renewals, as follows:

Term of Lease	Prescribed Percentage
30 years	nil
29 years	3.3
28 years	6.6
20 years	33.3
15 years	50.0
11 years	63.3

COMMENT: The basis for computation of the tax payable under S. 2(1) or 2(2) of the LTTA is "the value of the consideration for the conveyance". S. 18(2)(e) authorizes the making of regulations "providing for the method of calculating and ascertaining the value of the consideration in any case or class of cases".

In the case of a lease that is a taxable "conveyance" under the Act, the basis for the tax should be "the value of the consideration (given, or to be given by the lessee) for the conveyance (lease)". The objective of any formula or procedure adopted to determine that value should therefore be to arrive at a result that is, as nearly as may be possible as a practical matter, the present value of the lease payments to the extent those payments are reasonably referable to the use of the property, for the term of the lease, of the leased property. The portion of the lease payments reasonably referable to such use should be not more than the portion thereof that would be payable on a "net net lease" basis, as that term is generally understood in commercial leasing circles.

It will not always be practicable to determine the amount of such lease payments given the many forms of leases that will be encountered, many of which will involve variable payment formulae. Consequently, as a practical matter, it is felt that an alternative formula or approach is required. That suggested is based on the rationale that the value of any leasehold interest should, on a present value basis, be equal to the present value of the leased property to the owner, before subjecting it to the lease, minus the present value of the owner's right to regain possession of the reversion at the end of the lease term. To implement what is regarded by the Committee to be a practicable and reasonable application of this approach, it has arbitrarily been assumed that a lease for more than 30 years is equivalent, for purposes of the Act, to outright ownership of the property and that a lease for a lesser term represents a corresponding proportion of the present value of the leased property.

The Committee has assumed, in making this recommendation, that the Government will retain the 10 and 30 year exemptions now provided for leases by regulation.

RECOMMENDATIONS FOR INTREPRETATION BULLETINS UNDER THE LAND TRANSFER TAX ACT

Amalgamations:

23. RECOMMENDATION: An Interpretation Bulletin should be published to confirm that, in the case of a statutory amalgamation of two or more corporations, there is no transfer of any land owned by any of the predecessor corporations on the basis that there is no change of beneficial ownership. (A "conveyance" tendered to give effect to a change of name, for example, would not be taxable).

Transfer to trustee for corporation to be incorporated:

24. RECOMMENDATION: An Interpretation Bulletin should clarify the following points:

    1. A conveyance to the trustee is, when tendered, taxable.

    2. A subsequent conveyance from the trustee to the new corporation is, when tendered, not taxable.

    3. The resident status of the trustee will determine the tax payable on the conveyance to him (administrative procedures will be required to overcome any uncertainty as to that status preceding actual incorporation of the corporation).

Contributions of capital to corporations:

25. RECOMMENDATION: An Interpretation Bulletin should confirm that where land is transferred to a corporation as a contribution of capital, there is no consideration given by the corporation and the conveyance is therefore not taxable.

COMMENT: The kind of transactions contemplated involve contributions of capital (assets - in this case a transfer of land) to a corporation by one or more of its shareholders where no consideration is given by the corporation to the shareholder(s) in respect of the transfer. In accounting concepts, the value of the asset (land) received by way of such transaction is recorded in a "contributed surplus" account of the corporation. As a practical matter, such transactions will normally occur in situations where the corporation is wholly-owned, or very substantially owned, by the shareholder making the contribution. In other cases, where there is another significant equity interest involved, any accretion in value to that equity interest by reason of a "contribution of capital" by another shareholder will, in effect, be gratuitious - i.e. no consideration will flow to the contributing shareholder from the other equity interests.

Since, in transactions of this kind, there is

(a) no consideration in fact given for the transfer,

(b) usually (i.e. in wholly-owned subsidiary situations), no change in the beneficial economic interest in the land, and

(c) even if there is a partial change in the beneficial economic interest, it occurs gratuitiously - i.e. for no consideration,

it is submitted that complete exemption from the tax is appropriate.

RECOMMENDATIONS REGARDING FORMS UNDER THE LAND TRANSFER TAX ACT

26. RECOMMENDATION: Form 1. There should be added, in paragraph 1. of the Form, an additional sub-paragraph (and box) describing the deponent as an officer of the corporation that is the named transferee to which the land is conveyed.

The Land Speculation Tax Act, 1974

SUGGESTED AMENDMENTS

RECOMMENDATIONS FOR AMENDMENTS TO THE LAND SPECULATION TAX ACT

Distribution by trust in satisfaction of capital interest:

27. RECOMMENDATION: That the LSTA be amended in Section 1(1)(a)(i)(B) to provide for a rollover of designated land to a beneficiary where the assets of a trust comprising designated land are transferred to a beneficiary out of the trust in satisfaction of a beneficiary's capital interest therein.

COMMENT: In most situations, a trustee and the beneficiaries of the trust do not deal with each other at arm's length. As the Act is at present worded, the effect of the definition of "disposition", and "proceeds of disposition" would cause any gain occurring during the period of administration of the trust to be taxable at the time the designated land is distributed in specie to a beneficiary.

Family farm - adjusted value of designated land to transferee:

28. RECOMMENDATION: That the LSTA be amended to provide that Section 1(1)(a)(i)(C) should only apply where (D) relating to the family farm is not applicable.

COMMENT: The amendment is necessary to ensure that a choice is not available between the fair market value and the adjusted value in a non-arm's length sale. In an inter vivos transfer of a family farm, the adjusted value should be rolled over to the transferee and there should be no step-up in basis of the designated land.

The Family Farm - cost:

29. RECOMMENDATION: That Section 1(1)(a)(i)(D) of the LSTA be amended by removing the words "the adjusted value" on lines two and three and replacing them with the words, "the cost computed according to sub-clause A, or sub-clause (ii) whichever is".

COMMENT: Where a family farm passes from generation to generation under the Act as it is at present worded, the addition to the cost base contemplated by sub-clause (v) is computed on the adjusted value at the time of its first disposition. This includes the costs of improvements and the net maintenance costs whereas it is felt (if Recommendation 32 is adopted) these have already been provided for and it is felt that it would be inappropriate to allow the 10% compounded on these costs.

For example if A sells to B in 1990 after owning the farm for 10 years, and B holds the land for 10 years and A's adjusted value is:

Cost	$30,000
Improvements	20,000
Net Maintenance Costs	10,000
	$60,000

B would add to his adjusted value under Section 1(1)(a)(v) 10% of $60,000 compounded for 20 years. This recommendation would provide for the compounding to use as a base the cost of $20,000 and Recommendation 32 would provide for the improvements and net maintenance costs of A to be included in the adjusted value of B.

Rollover of designated land to members of the family:

30. RECOMMENDATION: That the LSTA be amended by adding a new section to the Act to provide that where an election is made on a prescribed form in connection with the disposition of designated land in Ontario between "members of the family" as that term is described in clause 1(1)(g) of the LSTA the amount stated in the election to be the proceeds of disposition shall be the adjusted value of the transferor and shall become the adjusted value of the transferee and the proceeds of disposition for the transferor.

COMMENT: The Committee is of the opinion that conveyances between "members of the family", as broadly defined, cannot be construed as speculative transactions. The policy objectives of the Treasurer as stated in the 1974 Ontario Budget are:

(a) designated to stablize prices

(b) discourage speculative activity, and

(c) the success of the tax will be inversely related to its revenue yield.

Therefore transfers of designated land between members of the family should be exempt and the adjusted value of the designated land to the transferor immediately before the transfer should become the adjusted value of the non-arm's length (member of family) transferee.

Adjusted value - neutral zone:

31. RECOMMENDATION: That the LSTA be amended to provide in Section 1 (1)(a)(ii) the amount to be included in the adjusted value is the greater of the fair market value on April 9th, 1974 or the actual cost to the transferor otherwise computed.

COMMENT: This amendment is required to ensure that in those situations where the value of designated land decreased between the date it was acquired and April 9th, 1974, tax does not become payable where the disposition does not produce any profit.

Transfer of farm land within the family:

32. RECOMMENDATION: That the LSTA be amended to provide in Section 1(1)(a)(iii) that the costs of improvements added by any previous transferor who acquired the land in a transaction to which clause (h) of Section 4 applied and who disposed of the designated land in a transaction to which clause (h) of Section 4 applied should be included in the adjusted value for the ultimate transferor who disposes of the designated land in a transaction to which clause (h) does not apply. A similar amendment to Section 1(1)(a)(iv) regarding net maintenance costs is necessary. (Another means of accomplishing the foregoing is to replace the word "first" appearing in the fourth line of sub-clause D of Section 1(1)(a)(i) with the word "last", but this alternative creates other technical problems.)

COMMENT: Section 1(1)(a)(i)(D) provides that where farm land is transferred within the family (including the farming corporation), the adjusted cost to the first transferor is passed on to subsequent owners. Section 1(1)(a)(v) provides for the 10% annual increment in value for the years during which the designated land was family-owned; however, any improvements made by any subsequent owners, or the net maintenance costs of any subsequent owners do not form part of the adjusted value.

For example, under the present wording of the Act, if a person sold a farm to his son, who passed it to his son (grandson of original transferor), the adjusted value to the grandson is the same as the grandfather's, without addition of the costs of improvements or net maintenance costs of the father.

Adjusted value - net maintenance costs:

33. RECOMMENDATION: That subsection 1(1)(a)(iv) of the LSTA should be amended to read as follows:

> for the period of time during which the transferor owned the designated land, commencing with April 9th, 1974 or the date of acquisition whichever is later, the lesser of either:
>
> (a) ten percent for each 12 month period, of the amount determined under sub clause (i) or (ii) whichever is applicable, or
>
> (b) the total net maintenance costs incurred by the transferor after the 9th day of April, 1974, with respect to the designated land.

Sub-clause (B)(2) should be removed.

COMMENT: A technical problem arises as the section is now worded in that the aggregate of all the net maintenance costs for all years the designated land was owned is added to the adjusted value for each year the designated land is owned. The words "the aggregate of" become unnecessary when Section 1 (1)(a)(iv)(B)(2) is removed. (See Recommendation 39 for comment on why this sub-clause should be removed.)

Limitation of net maintenance costs; indexing for inflation:

34. RECOMMENDATION: That the government review the adequacy of the percentage provided for in Section 1 (1)(a)(iv)(A) in the light of current interest costs.

In the alternative, an allowance should be given which is indexed in some manner to the general rate of inflation. Such addition to adjusted value could be tied to the increase in consumer price index for Canada or the current building index published by Statistics Canada over the period during which the land has been held in much the same manner as has been provided for increased exemptions in Section 117.1 of the Income Tax Act (Canada).

That the LSTA be amended in Section 1 (1)(a)(v) by adding that a retired farmer should be allowed the benefit of the 10% compounding feature if he rents his farm to be used in farming. To obtain this benefit, it would be a requirement that the transferor must have farmed the designated land for a minimum period of five years prior to his retirement.

COMMENT: Section 1 (1)(a)(iv)(A) restricts the addition of net maintenance costs to the adjusted value to an annual maximum of 10% of the cost as determined in sub-clause (i) or (ii). At the present time the annual allowance of 10% would not cover interest costs of holding land and other maintenance costs. Section 1 (1)(a)(v) is intended to reflect the increased value attributable to inflation. Genuine farmers who retire and use their farm as their source of retirement income should be allowed the allowance for inflation and therefore it would appear desirable to provide a continuance of the indexing factor for retired farmers who rent their land for farming purposes.

Canadian Resource Property:

35. RECOMMENDATION: That the LSTA be amended in Section 1(1)(b) so that the concluding words state as follows: "but 'designated land' does not include any land in Ontario that is, within the meaning of paragraph c of subsection 15 of Section 66 of the Income Tax Act (Canada), were that paragraph read without reference to the year '1971', 'Canadian resource property' or any interest held in land solely as security for some indebtedness secured by the land."

COMMENT: The definition of "Canadian resource property" in paragraph 66(15)(c) of the Income Tax Act (Canada) pertains to property acquired by the taxpayer after 1971. In our view, land in Ontario which is a Canadian resource property whenever acquired should be excluded from the definition of "designated land".

"Disposition" - Leases:

36. RECOMMENDATION: That the LSTA be amended in Section 1 (1) (d)(iii) by adding immediately after "any such lease" the words "where the term remaining including any renewals or extensions thereof may exceed 10 years".

COMMENT: As the definition of disposition is presently worded with respect to leases, a disposition of any interest in a lease which was originally for more than 10 years but which has less than 10 years to run is a disposition which is subject to tax. In the Committee's view, the subsequent sale, assignment or transfer of rights under such a lease should not be included in the definition of "disposition".

See our additional commentary on leases on pages 84 to 89.

Valuation:

37. RECOMMENDATION: That the LSTA be amended in the various sections which refer to "value" or where value is not mentioned as in Sections 1 (1)(d)(v), (vi), and (vii) with respect to the 50% asset test for designated land. The term employed should be "fair market value".

COMMENT: In view of the fact that value may have many meanings such as book value, tax value, net asset value, etc., it is recommended that for clarity and greater certainty the term "fair market value" which is defined as the "highest price, estimated in terms of money which a willing seller may obtain for the property in question in an open and unrestricted market from a willing and knowledgeable purchaser acting at arm's length", be employed.

In those sections of the Act where the 50% asset test is used, it should be eminently clear that the test is 50% of the fair market value of all of the assets of the person holding the designated land.

Net maintenance costs of farmers:

38. RECOMMENDATION: That the LSTA be amended to provide in Section 1(1)(j) that a farmer whose chief source of income is from farming or a combination of farming and some other source, is not required to reduce his net maintenance costs by any income earned from the land. We further recommend that an Interpretation Bulletin be issued on net maintenance costs of farming.

COMMENT: This amendment is necessary to ensure that where a loss is incurred, the net maintenance costs will not be reduced by any income earned. The addition of the "combination of incomes" should ensure that the true farmer is not inadvertently classed as a "hobby-farmer" under this Act because losses are incurred in a particular year.

The amendment is also necessary so that a farmer starting up his business, and having outside employment to provide working capital, is not precluded from adding net maintenance costs to his adjusted value.

The section also creates an absolutely insoluble problem in determining the income attributable to the transferor's own use of land. Except where rental is involved, the Committee is of the view that no income should be imputed to the transferor from the use of the land. Consideration should also be given to the whole concept of adding to the adjusted value any amount for maintenance as it is felt these ongoing costs are consumed and are not at all like costs of improvements which add value.

Adjusted value and proceeds of disposition - clarification of limitation of net maintenance costs and costs of disposition:

39. RECOMMENDATION: That the LSTA be amended to provide that in Section (1)(1)(1) the "proceeds of disposition" be restated as the net consideration received after deducting costs of disposition. It is further recommended that an Interpretation Bulletin be issued to clarify the terms "cost of acquisition", "costs of improvements", "costs of disposition", etc.

COMMENT: It is normal in any computation of profit to deduct the costs of disposition. As Section 1(1)(a)(iv) now reads a part or all of the costs of disposition falling under sub-clause (B)(2) could be disallowed because of the 10% limitation in sub-clause (A). As well there does not seem to be any reason to disallow a portion of the expenses relating to the valuation of the property as of April 9th, 1974.

Joint Tenancy:

40. RECOMMENDATION: That the LSTA be amended in Section 1(1)(1) by removing in the penultimate and last lines of the Section the words "under the last will and testament of any person or on the intestacy of any person" and substituting therefore the words "as a result of the death of any person".

Also that Section 1(1)(a)(i)(B) of the LSTA be amended by removing the words "under the will or on the intestacy of a person" and replacing them with the words "as a result of the death of any person".

This sub sub-clause should be further amended by adding the words "and for greater certainty the land deemed to be acquired as the result of a death of any person which was held in joint tenancy shall be deemed to be that portion of the designated land in which the deceased person had a beneficial interest immediately prior to his death".

COMMENT: Under the provisions of the LSTA designated land passing on the death of a transferor under his will or by intestacy is a disposition, but since no proceeds of disposition arise, it is not a taxable transaction. Furthermore, persons acquiring designated land under a will or by intestacy of any person should acquire such land at a stepped-up cost base equal to the fair market value at the date of death of the transferor. However, the most common form of ownership of land in Ontario is joint tenancy and the amendments noted above would accord the same exemption and step-up in base of adjusted value to land passing as a result of the death of a joint tenant as the existing legislation provides as a result of the death of a person who has outright ownership of designated land in Ontario.

Disposition by trusts:

41. RECOMMENDATION: That Section 1(1)(p)(ii) of the LSTA be amended to provide that where designated land is disposed of by a trust, the trust shall be deemed to be the transferor disposing of the beneficial interest in designated land.

COMMENT: In many cases, there are no ascertained specific beneficiaries of a trust which holds designated land. In other cases there are both income and capital beneficiaries of a trust and proceeds of disposition of trust property are to be held in trust for various purposes until a later date upon which the capital beneficiaries are to take their share. As the LSTA is at present worded, it would seem that the capital beneficiaries would be liable for the tax even though they may only have a contingent interest in designated land held by the trustees of the trust.

This section in its present form could conceivably also become unworkable in the situations of real estate investment trusts (REIT's) and unit trusts.

There seems to be no reason why the land speculation tax, if applicable, could not be paid by the trust itself and the trustee could then determine, on the basis of the "even hand" rule, how the tax is to be apportioned among the beneficiaries.

Control - Definition:

42. RECOMMENDATION: That Section 1(5) be repealed and in lieu thereof a provision of the following effect be substituted. For the purpose of the LSTA, "control" of a corporation means control whether through holding a majority of the shares of a corporation or any other manner whatsoever, and the word "controlled" has a comparable meaning.

COMMENT: The present definition is imperfectly worded. The definition set forth above is adopted from the definition contained in the pre-1972 Income Tax Act (Canada) with respect to a personal corporation. A "control test" is required for purposes only of sub-clause (vii) of clause (d) (as amended by our Committee's suggestions and observations) and for the purpose of Section 2(2).

Time of disposition:

43. RECOMMENDATION: That for the purposes of the LSTA and more specifically Section 2(3) thereof, it should be made abundantly clear when in fact the disposition occurs. A disposition should arise only when the acquirer takes possession of the designated land or assumes the incidence of title thereto.

That the definition of "disposition" be redrafted to make it clear that a disposition only arises when the transferee takes possession of the designated land or assumes the incidence of title, as previously mentioned.

COMMENT: Our Committee is concerned that it is not entirely clear when a disposition takes place. For example, at the time of entering into an agreement of purchase or sale or at the time of "closing" of the transaction.

In this connection, it should be made clear that the entering into of a conditional agreement of purchase and sale is not to be considered a disposition until such time as the conditions have been met or waived or the purchaser has all of the incidence of title. (See, for example, Wardean v. M.N.R. 69 DTC 5194).

A disposition should only arise in respect of the exercise of an option at the time when a conveyance is delivered or other acts of ownership by a purchaser are exercised as in the case of an agreement of purchase and sale. On the sale or assignment of an option in respect of designated land, a disposition should be considered to have arisen at the time the consideration for the sale or assignment is payable.

Principal residence - ten acres:

44. RECOMMENDATION: That Section 4 (e) of the LSTA be amended to provide that when the designated land disposed of is the principal residence of the transferor, there should be an exemption of the subjacent and immediately contiguous land not exceeding 11 acres (rather than 10 acres).

COMMENT: For many years, the Planning Act of Ontario has required that a parcel of land must have more than 10 acres to be exempt from its application. Therefore, many of the rural conveyances in Ontario have had fractionally more than 10 acres but rarely more than 10.5 or 11 acres.

This amendment would resolve what might otherwise be an inequitable result and would reduce considerably the administrative difficulties of dealing with principal residences of slightly more than 10 acres.

Adjusted value - transfer of family farm on death:

45. RECOMMENDATION: That LSTA be amended to provide that Section 4(h) applies only to transactions otherwise than on the death of the transferor.

COMMENT: The intention of the Act is to allow a step-up in cost base of designated land where the transferee acquires land as a result of the death of the transferor. This same treatment should be accorded to farmers, and it would appear under the present wording of the Act that Section 4(h) and Section 1(1)(a)(i)(D) would restrict the adjusted value of the beneficiary to that of the deceased.

Farming Corporation:

46. RECOMMENDATION: That the LSTA be amended to provide an exemption in Section 4(h), where the transferor of a designated land is a farming corporation and the disposition of such land is to a shareholder or to a member of the family of the shareholder of the farming corporation.

That the LSTA be amended to provide in Section 1(1)(g) that a farming corporation be deemed to be a member of the family of the shareholders for the purposes of Section 4 (h) and the definition of farming corporation in Section 1 (1)(f) include corporations which acquire land for use in farming, or which held land used in the business of farming on April 9th, 1974.

COMMENT: The present legislation contemplates exemptions for intra-family transfers of the family farm. The Act also pierces the corporate veil where it is clear the corporation is used solely to hold the family farm. Therefore, provision should be made for the corporation to transfer the designated land to members of the family without having to transfer shares or wind-up the farming corporation. As well, the definition of the farming corporation only contemplates the situation where the family farm is "incorporated" after April 9th, 1974 and does not include those corporations which acquire farm land in arm's length transactions.

Expropriation:

47. RECOMMENDATION: That Section 4 of the LSTA be amended by deleting clauses (i) and (j) which exempt government purchase or expropriation transactions from a tax otherwise payable if the transaction were with a private party. Instead, alternative relief should be provided in the form of a potential rollover, which would put the owner in the same position after the transaction as he was before, rather than in a better position as now provided.

COMMENT: Our Committee feels strongly that the provision of the preferred tax treatment of land transactions with the Ontario Government inherent in Section 4 (i) and (j) has created a situation which may adversely affect the future of the housing and land development industry in Ontario. This exemption from tax on transactions with government provides a mechanism when coupled with the Ontario Land Corporation for a substantially increased role by government in land development and a severe tax disincentive for transactions with anyone other than government. Each and every land transaction with government which might otherwise attract the 50% land speculation tax would be under a cloud of suspicion. Every transaction with government in designated land would carry with it not only a purchase price at fair market value but also a tax exemption. In effect, unless our recommendation of deleting clauses (i) and (j) of Section 4 is accepted, there would be created a potential two-price system in all Ontario land. On the grounds of horizontal equity from a tax policy viewpoint, these exemptions for government purchase or expropriation transactions should be repealed.

The solution to the Land Speculation Tax Act problems in this respect can be overcome by permitting deferral of the tax on a rollover basis. This means that if within a specified period of time, say 12 to 18 months, the persons selling to government or whose land was expropriated by government re-invests the entire proceeds in land, the tax is deferred until the replacement land is sold. The deferral of gain on involuntary dispositions is not novel in Ontario taxing statutes; for example, the same type of tax policy issue is dealt with in a comparable manner in Section 46 of the Ontario Corporations Tax Act.

Institutional investors:

48. RECOMMENDATION: That a new subsection be added to Section 4 to provide that where a "financial institution" (as defined in the regulations) disposes of designated land, it is an exempt transaction provided that it is established that

(a) the mortgagor and mortgagee were dealing at arm's length,

(b) the foreclosure was effected for the purpose of safeguarding the rights or interests of the mortgagee in respect of a loan made by him, the whole or any part of which is outstanding, and

(c) neither the giving of the mortgage nor the foreclosure in respect thereof was carried out for the purposes of avoiding payment of tax under Section 2(1).

COMMENT: A mortgage investor is in the business of lending money on the security of mortgages on land, not in speculating in land acquired through foreclosure. It is not an uncommon situation that a loan will fall into arrears although it is not frequent with those institutional investors who take time to investigage the credit worthiness of the borrower. When it does happen, the investor's objective is to dispose of the property to recover his investment, not to speculate. While profits sometimes occur on the subsequent disposition, more often losses occur and the Act does not provide for the netting of gains and losses. The cost base also does not provide for the administrative and management costs involved so the computation of profit is questionable.

The regulations should define "financial institutions" (see Recommendation 58A).

Affidavit for release of lien:

49. RECOMMENDATION: That the affidavit under Section 5(3) of the LSTA should be expanded to cover the exemption provided for in Section 21 of the LSTA.

The affidavit should also be expanded to permit a statement by an officer of a corporation that no tax is exigible under Section 2(2) of the LSTA. A paragraph should be added whereby the transferor may verify that during the time the corporation owned the land, none of the events set out in Section 1(1)(d)(v), (vi), or (vii) occurred, or that the corporation did not, during the time that it held the land have 50% or more of its assets in designated land.

The affidavit should also be applicable to mortgages so that no lien clearance certificate need be required with respect to tax under the deemed disposition provisions of Section 2(2) of the LSTA.

COMMENT: In the view of the Committee, a purchaser should be able to rely on the Registry or Land Titles Acts in ascertaining liens. It is noted that the affidavit will eliminate the lien itself, although not the tax.

Under the existing wording of Section 5(3) of the LSTA (a) a lien clearance certificate will always be required for transactions under Section 21 of the LSTA pertaining to subdividers, (b) a lien clearance certificate is necessary in all transactions with corporations in view of the provisions for deemed dispositions contained in Section 2(2) of the LSTA. In the future, the problem will become more pronounced with respect to past transactions which took place since April 9, 1974 without certificates being attached.

Implementation of this recommendation should be effected with the co-operation of the Property Law Branch of the Ministry of Consumer and Commercial Relations.

Lien Clearance Certificate:

51. RECOMMENDATION: Generally the concept should be that of following the existing registry and land titles system. If the clearance certificate is registered on title there should be no lien affecting the land in existence up to the date of clearance given in the certificate.

COMMENT: A bona fide purchaser for value without notice must be able to rely on the title of the property as found in the Registry or Land Titles Office.

Where a transferor disposes of designated land which is exempt from tax pursuant to the provisions of Section 4 of the Act and the transferor appends to such disposition his affidavit in the prescribed form invoking such exemption provision and the Land Registrar accepts and registers such disposition, then subsequent purchasers for value of such designated land shall be entitled to assume that such disposition is exempt from tax.

Investment Properties held prior to April 9th, 1974:

51. RECOMMENDATION: That Section 20(2) of the LSTA be amended to read as follows: "where, after the 9th day of April, 1974, designated land that is an investment property is disposed of and the designated land has been an investment property of the transferor or members of his family as defined in subsection 1(1)(g) of the LSTA, the taxable value, computed as if this section were not applicable, of the investment property so disposed of shall be reduced by an amount equal to 1/10 thereof for each full year during which the investment property disposed of was an investment property owned by the transferor or members of his family".

COMMENT: Section 20(2) provides for a reduction in tax in respect of investment property used for residential purposes. The reduction is only applicable if the property is sold after April 9, 1977 so that any person who sells such a property between April 9th, 1974 and April 9th, 1977 will be subject to full tax even though the person had held the property for considerably more than a ten-year period. A person holding the same property for a period of ten years after April 9th, 1974 would under the revised wording be completely exempt from tax. The same pro-rated reduction of tax should apply if the property has been held for the relevant number of years whether the investment property was acquired prior to or subsequent to April 9th, 1974.

The Committee's view is that transactions in designated land between members of a family are not speculative and therefore there should not only be a rollover of the adjusted value of the land with no tax exigible (see Recommendation 30) but the "credits" under Section 20 of the LSTA for the years the property was retained in the family should also flow through to the transferee.

Subdividers' sales of land to builders:

52. RECOMMENDATION: That Section 21 of the LSTA be amended to provide that where a transferor has subdivided and either serviced or provided for the servicing of designated land in accordance with the requirements of a "sub-division agreement" (to be defined in the Regulations) between a municipality or other governmental body and the transferor, which is enforceable against the transferor by the municipality or other governmental body and where it is a condition of the agreement for sale that a deed or other form of conveyance will not be delivered and title will not be required to be transferred until a building permit is available for construction on the designated land, such a transfer shall be exempt.

COMMENT: Section 21 of the Land Speculation Tax Act, 1974 was added to the Act during clause-by-clause debate in order to permit the sale of designated land on an exempt basis by land developers and subdividers to the small independent builder.

In the view of the Advisory Committee the stipulations in Section 21 will further reduce the sale of serviced lots to independent builders and will concentrate the construction of residential housing in the hands of a few larger fully-integrated land development companies. To this extent Section 21 is counterproductive.

It is doubtful if a builder would assume an unknown or unquantified liability for tax as is required by the present wording of Section 21 of the LSTA.

In most cases, the developer will not wish to disclose his costs (and thereby his profits) before the negotiations are completed and in any event he will be unable to ascertain his costs as of a given date for a particular piece of designated land in a proposed subdivision. Determination of the cost of a particular piece of land is further complicated because the costs of subdividing and servicing in a subdivision, including the cost of land dedicated for roads and municipal purposes, usually are allocated to particular parcels of land on an arbitrary basis.

Sometimes it is necessary for the vendor of lots to repossess them under the terms of the sale agreement, or a mortgage given by the purchaser at the time of sale. Complications will arise on subsequent resales if tax liens are registered on title because construction of buildings had not commenced within the required 9 or 18-month periods. There is no indication of what will constitute

commencement of construction under Section 21 and it would be difficult to define such commencement in a regulation to the LSTA.

The time limitations of commencement of construction of buildings within nine months immediately following the disposition of at least 50% of the building sites or lots included in a designated land and within eighteen months immediately following the disposition commencing construction of buildings on the remainder of the sites appears impractical in view of time periods often required for obtaining financing, satisfying municipal requirements for site planning, etc. Furthermore, if the time limitations required in existing Section 21 commence from the date that an agreement for sale is signed, it does not recognize the market practice of pre-selling lots to builders and ignores the existing type of covenant usually set out in a standard sales agreement. Moreover, the time limitations may not be practical in the current market conditions. The Committee considers it unlikely that there would be undue speculation by persons who acquire building sites or service lots but refrain from commencing construction thereon. Subdividers usually require construction within a stipulated period of time in order that they will be released from their obligations in the subdivision agreement at the earliest possible time. In the view of the Committee, other market forces and conditions, including real estate carrying costs, could also mitigate against such a practice.

The lien that is imposed by Section 21 (2) will create a severe hardship for builders since it will have priority over any mortgage given back by the builder to the subdivider vendor. The effect of the lien may be to eliminate bridge financing and may come ahead of any mechanics lien that may be placed by a sub-contractor or supplier of materials.

It is for all of these complications and for other valid reasons that this recommendation is being made for a broader exemption of a subdivider who sells serviced land.

Any subsequent sale by the purchaser of the lands would have to meet the tests of "value-added" to obtain an exemption from the land speculation tax and if the land was sold without the required value being added, the subsequent vendor would be subject to tax on his gain.

Although it has been recommended that subdividers be exempt from the tax, it is not recommended that severances granted by a Committee of Adjustments or otherwise be exempt. The reason for this is that the owner of a single undeveloped lot would be taxed on resale and it is felt that it would be unfair to allow a seller of one or more single undeveloped lots to be exempt simply because these lots were created by means of a severance. It is anticipated that

a party severing land and doing whatever a subdivider would be required to do would be exempted as being a subdivider. Therefore, the subdivision agreement definition should exclude severances.

The Committee is of the opinion that before a land development or subdivision transaction could be exempt from tax, there should be a significant addition of economic value to the designated land. We believe that the recommendation set out herein does require the necessary addition of economic value to the designated land by the installation of services, etc.

Change of use - principal residence:

53. RECOMMENDATION: That Section 22 of the LSTA be completely redrafted and be replaced with a "change of use" rule which would provide an exemption during the period which the designated land was used as a principal residence. This provision would apply not only to those taxpayers whose age is in excess of 65 years but to all taxpayers.

COMMENT: Section 22 of the LSTA provides an exemption for a person 65 years or older who disposes of a principal residence that he held for at least five years. However, the general scheme of the LSTA provides that principal residences should be exempt and it seems within the spirit of the Act to extend this exemption to all persons. In addition, a "change of use" rule should be introduced whereby the cost base of the designated land would be stepped-up to the fair market value at the time of the change of use of such designated land.

This "change of use" rule should provide for the situation where a principal residence is changed to commercial or to investment property use. Where the reverse is true and an investment property or a commercial property is changed to a principal residence, there should be a deemed disposition at the fair market value at the time of change of use.

It would be very easy as the LSTA is presently drafted for a transferor of designated land which is an investment property but which has not yet achieved the full exemption, to move his family into the property for a short period so that at the time of its disposition it would be considered his "principal residence" and thereby be exempt. The "change of use" rule would close this potential loop-hole in the LSTA as it presently exists.

The tax which might be exigible as a result of the deemed disposition could cause hardship and therefore security in lieu of payment of the tax should be considered by the LSTA administration.

RECOMMENDATIONS FOR REGULATIONS
UNDER THE LAND SPECULATION TAX ACT

Commercial or industrial - predominant use:

54. RECOMMENDATION: That a regulation be issued by the Lieutenant Governor-in-Council under the provisions of Section 23 (2)(b) of the LSTA providing that where a property is used partly for commercial and industrial use and partly for some other purpose, and the proportion of proceeds on a disposition that is reasonably allocable to the buildings is 40% or more of the proceeds, then the proceeds of disposition and the adjusted value shall be reduced by an amount equal to the proportion of the total that is reasonably allocable to the industrial or commercial use.

COMMENT: In many smaller cities and towns in Ontario, it is a common situation to find apartments over stores. As well, in the larger cities, it is becoming common to mix commercial property and apartment properties. The above recommendation would provide a partial exemption for the portion of the property used for industrial or commercial use. The balance of the property would then be treated as an investment property according to Recommendation 55 and be accorded a partial exemption as provided in Section 4(d).

Investment property - partial use:

55. RECOMMENDATION: That a regulation be issued by the Lieutenant Governor-in-Council under the provisions of Section 23 (2)(b) providing that where a designated land is used partly as an "investment property" and partly for some other use, the portion of the proceeds of disposition and adjusted value that are reasonably attributable to the investment property shall be treated as a disposition of an investment property under Section 20 of the Act.

COMMENT: This regulation is the corollary of Recommendation 54 and is necessary to ensure that partial uses of one property are accounted for according to the general principles of the Act and that transferors are not penalized because the property in question is a hybrid of commercial/industrial on the one hand and investment property on the other hand.

Consideration might, however, be given to the question of whether a "de minimis" rule should be applicable before the allocation principle is invoked.

Carrying costs - resale properties, home rehabilitators:

56. RECOMMENDATION: That a regulation be issued by the Lieutenant Governor-in-Council under the provisions of Section 23 (2)(j) of the LSTA defining the words "costs of improvements" in Section 1(1)(a)(iii) to include carrying costs including municipal taxes, interest paid on mortgages and insurance where designated land is purchased with the intention of resale.

    The conditions which must be met for this to apply would be that part of the ordinary business of the transferor is the buying and selling of designated land in Ontario and that the profits from these transactions are included in income from business for income tax purposes.

COMMENT: Home rehabilitators who buy properties with the specific intent of renovating the buildings acquired and reselling them incur carrying costs for these projects while under renovation. These costs include municipal taxes, interest paid on mortgages and insurance. The "net maintenance cost" provisions of the LSTA do not adequately provide for these expenses. Wherever the property is acquired for the purpose of renovation and resale, the computation of the true economic gain should take into account all of the costs applicable thereto while the property is held.

Costs of improvements:

57. RECOMMENDATION: That a regulation be issued by the Lieutenant Governor-in-Council under the provisions of Section 23(2)(j) to define the words "costs of improvements" in Section 1(1)(a)(iii) to include a reasonable amount for the value of the labour actually performed by the transferor in connection with such improvements provided the transferor is not a corporation.

COMMENT: This regulation is necessary to ensure that the Act does not discriminate against an individual in favour of a corporation. Where a corporation pays wages that are reasonably allocable to improvements they would be included in the cost of improvements and the same treatment should be accorded to an individual.

Tourist resort:

58. RECOMMENDATION: That the Ministry of Tourism of Ontario be consulted to determine the class, kind or designation of tourist resort that is to be exempted from any tax under Section 4(d) of the LSTA.

COMMENT: Section 4 (d) provides for an exemption of tourist resort of a class, kind or designation to be prescribed. In the view of the Committee, the Ministry of Tourism is the most appropriate governmental body to suggest the prescription of the class or kind of tourist resort to be exempt. The class, kind or designation of tourist resort to be exempted should be clearly stated and the exemption should not be discretionary.

Home rehabilitators and conversion to condominiums:

59. RECOMMENDATION: That a regulation be issued by the Lieutenant Governor-in-Council under the provisions of Section 23 (2) (j) defining the costs of renovations for the purposes of Section 4 (g)(ii) to include at least the following categories of expenses:

(1) Renovation costs which would include all payments for structural and cosmetic repairs, including wages or salaries paid to onsite foremen or supervisors, architects fees, planning fees, engineering fees, and surveying costs, mortgage repayment penalties, mortgage application fees, mortgage insurance fees, mortgage brokerage or commissions and special front-end bonuses.

(2) Where the renovation costs as defined in (1) above amount from $0 - $200,000 an allowance of 5% of the renovation costs should be included in renovation costs as overhead, where the renovation costs are from $200,000 - $400,000 the overhead percentage should be 4%, from $400,000 - $600,000 - 3% and over $600,000 - 2%.

COMMENT: Section 4 (g)(ii) exempts the designated land from tax where the transferor has renovated a building at a cost of not less than 20% of his "cost" and the buildings or other structures have a value at the time of disposition of not less than 40% of the total proceeds.

This section of the LSTA would apply to renovations of homes by both individuals and renovation companies and could also apply to rental accommodation that is converted and sold as condominiums.

Consideration must be given to what is included in the definition of cost which would make up the 20%. In both the renovation of older homes and in the conversions of rental accommodation into condominiums there are considerably more expenditures than just the physical changes. Depending on whether the project is a large or small one, there could be such costs as architectural, planning and engineering fees, and in the case of a condominium conversion, surveying fees. These latter fees can be very expensive.

There are also many costs involved in replacing the old mortgage on the property with new financing. In this category there could be penalties for repayment of an old mortgage, and in arranging a new mortgage there would be brokerage fees or commissions, mortgage application fees, mortgage insurance fees, and even in some cases a special front-end bonus.

There is one other cost that should be reflected in the 20% and that is overhead. In the case of a large company doing the renovations there will be a certain amount of head office overhead that should be allocated to the project even though the project may be only one of many being carried out by the company. In the case of small projects carried out by individuals it is not uncommon for the owner to put substantial work and effort into the project for which there is no charge for his own time and effort.

It is virtually impossible to arrive at a method that would satisfactorily allow for actual overheads to be charged either in the case of large corporations where the project is one of many or in the case of an individual person doing his own renovation. However in our view some factor for overhead should be allowed on sliding scale in respect of renovation costs.

At the time of disposing of the renovated property there would be selling costs such as real estate commissions, advertising and legal fees and it has been recommended elsewhere in this report (see Recommendation 39) that these costs be taken into account in net proceeds.

Subdivision agreement:

60. RECOMMENDATION: That a regulation be issued by the Lieutenant Governor-in-Council under the provisions of Section 23(2)(j) to define certain expressions for the purposes of Section 21 of the Act:

(1) "subdivision agreement" means

(a) any agreement referred to in clause (d) of subsection (5) of Section 33 of The Planning Act, and

(b) any other agreement concerning land development or relating to the creation of building sites or lots entered into between a transferor and a municipality

provided that, in each case, provisions shall be made in such agreement for the construction of required services or other improvements adding economic value to the designated land.

(2) A subdivision agreement in respect of designated land shall be deemed to be between a municipality and the transferor and enforceable against the transferor if it has been entered into by or on behalf of the registered owner of the designated land.

(3) Designated lands comprising a building site or lot shall be deemed to have been serviced when the transferor has performed its obligations under a subdivision agreement to the extent necessary to permit the issuance of a building permit in respect of such building site or lot, if applied for.

(4) Designated land comprising a building site or lot shall be deemed not to have been disposed of until any conditions in the agreement for sale relating to the availability of a building permit for such building site or lot shall have been satisfied by the transferor.

Financial institutions:

61. RECOMMENDATION: That a regulation be issued by the Lieutenant Governor-in-Council under the provisions of Section 23(2)(j) of the LSTA defining "financial institutions" for the purposes of Section 4 to include banks, trust and loan companies, insurance companies, investment trusts and other persons, part of whose ordinary business includes the lending of money on the security of a mortgage on real property.

COMMENT: Recommendation 48 provides for an exemption for certain financial institutions which acquire designated land through foreclosure and subsequently dispose of it. It is necessary to control who falls within the ambit of this expression; this can be accomplished by defining "financial institutions". The definition, however, should be sufficiently broad that mortgage lending activity in Ontario by institutional investors will not be adversely affected.

Commercial or industrial purposes - notch provision:

62. RECOMMENDATION: That the Lieutenant Governor-in-Council issue a regulation under the provisions of Section 23 (2)(k) of the LSTA to provide that where the costs of improvements, structures or other capital improvements to a property are less than 40% of the proceeds of disposition and the property would be exempt under Section 4 (d) of the Act if they exceeded 40%, then the tax payable under Section 2 (1) should be reduced by a factor representing the percentage of value attributable to the disposition of the land or buildings.

COMMENT: It seems inappropriate to tax fully a transaction where the 40% or more test is not completely achieved. Therefore, it is envisaged that the tax would be reduced as follows:

$$\text{Tax at 50\%} \times \frac{\text{percentage achieved}}{40} = \text{tax reduction}$$

RECOMMENDATIONS FOR INTERPRETATION BULLETINS UNDER THE LAND SPECULATION TAX ACT

Long term lease of farm land:

63. RECOMMENDATION: An Interpretation Bulletin is necessary to clarify the definition of commercial lease to ensure that the lease of designated land which is farm land in Ontario falls into this category.

COMMENT: Section 1(1)(d)(iii) would cause owners of land to give up leasing it for long-term agricultural use if the transaction caused tax to be exigible. Therefore, it should be made absolutely clear that farming is considered a commercial use permitting lease of farm land for 30 years or less to be exempt under Ontario Regulation 469/74.

Farming - chief source of income:

64. RECOMMENDATION: An Interpretation Bulletin should be issued confirming that where the transferor's chief source of income is farming or a combination of farming and some other source of income these words should be interpreted as in James v. MNR (73 DTC 5333) and Dorfman v. MNR (72 DTC 6131) to make it clear that the expectation of income and the amount of time expended are the governing factors not "net income".

COMMENT: Recommendation 38 mentions the fact that many farmers require additional income to provide capital, or in some cases, to provide enough income to live in a reasonably comfortable manner. In rural Ontario, it is common to take on part-time employment such as driving school buses, or construction work and the industry displayed by these individuals should not be penalized by the LSTA by the denial of the addition to the adjusted value in respect of "net maintenance costs".

Farming carried on on designated land:

65. RECOMMENDATION: An Interpretation Bulletin should be issued in connection with Section 1(1)(a)(v) that where a farm is being worked by any member of his family, the transferor will be considered to be an employer (whether or not wages are actually paid) and will therefore also be considered to be carrying on farming for the purposes of this sub-clause. This might apply, for example, where a farmer retires and his son continues to carry on farming the father's land.

The bulletin should also confirm that the practice of hiring or contracting the ploughing, seeding, harvesting, and so on, where the risk of the profit or loss from the crop lies with the owner shall also constitute farming.

COMMENT: Considerable comment has been made that some traditional arrangements, such as those mentioned above, would not be considered farming and therefore the compound factor in Section 1(1)(a)(iv) would not apply.

Costs of disposition, "net proceeds of disposition":

66. RECOMMENDATION: An Interpretation Bulletin should be issued to confirm that the "costs of disposition" should include obtaining severances (if not included in "costs of improvements), legal fees, real estate commissions and the cost of obtaining a valuation of the designated land if the property was owned on April 9, 1974.

COMMENT: It is not clear at the moment what costs will be permitted under the LSTA. It could also be costly to obtain valuations as of April 9, 1974 and therefore the Committee feels some guidelines are necessary.

ERRATA

Page 41: THIRD LINE FROM BOTTOM OF PAGE should read:

"to use as a base the cost of
$30,000" NOT --- $20,000

Page 60: LAST LINE should read:

"Recommendation 61)". NOT --- 58A

"Costs of improvements"

67. RECOMMENDATION: An Interpretation Bulletin should be issued to confirm that "costs of improvements" include such items as costs incurred for severances and subdividing under the Planning Act (Ontario), and for servicing designated land.

COMMENT: See Recommendation 66.

Cost of acquisition:

68. RECOMMENDATION: An Interpretation Bulletin should be issued to confirm that the definition of "cost of acquisition" includes legal fees, transfer tax (whether the regular rate or the 20% rate), and other expenses related to the acquisition.

COMMENT: See Recommendation 66.

LEASES

TAX IMPOSED UNDER LSTA ON DESIGNATED LAND DEEMED TO BE DISPOSED OF WHEN LEASED FOR A PERIOD THAT MAY EXCEED TEN YEARS

In implementation of the policy of the government to curb speculation in land, consideration must be given to leasing, since it is possible to effectively change ownership of land by entering into long-term leases. However, the situations where tax would be avoided, would likely be short term leases, at exorbitant rents with an option to buy at a deflated price, and this type of gimmick can be effectively stopped by the anti-avoidance sections. The Committee feels that speculation is more likely to arise when a lessee disposes of his leashold interest as opposed to the initial leasing of designated land by the owner thereof.

The Committee also spent considerable time trying to envisage those lease situations which would not be exempt by Section 4(d) and Ontario Regulation 469/74.

Problems of valuation relating to determining the amount constituting the proceeds of disposition of determining whether leased premises, where less than the entirety of a property is leased, meet the 40% test for Section 4(d), and determining the adjusted value of the designated land disposed of, are in the Committee's view, almost insoluble.

The disposition by way of lease, of raw land or of serviced land, which does not contain buildings, is certainly a transaction which might be considered one to which this Act should apply. However, we feel that this overlooks a common method of obtaining financing which is to either lease the land to a developer and agree to lease back a completed building built to specifications of the intended lessee or to construct the building and enter into a sale leaseback agreement. We do not feel it is the government's intention to inhibit ordinary commercial transactions of this sort, and conclude

that even the long-term lease of land should, in most cases, be exempt from land speculation tax. Those lease situations which are clearly designed to avoid the tax should be dealt with by an anti-avoidance section.

For all of the foregoing reasons, the Committee strongly recommends the government exempt the initial leasing of any designated land in Ontario and tax only the sub-leasing or sale of leasehold interests. Should leakage develop in the tax system which the Committee feel is doubtful, then revised rules for leasing can be implemented to control the problem. In this connection, the Committee is studying further the "Development Gain Tax" in the United Kingdom where leaseholds as opposed to freeholds, are the most common form of ownership.

Since sub-leases and assignments of leases, even if the Committee's broad recommendation for exemption is not adopted and all leases (save those exempted by the legislation) are to be considered transactions which might create a taxable disposition, the following recommendations are made.

Lease: Exemption where lessee covenants to construct

69. RECOMMENDATION: That the LSTA be amended to provide an exemption for the initial leasing of designated land if the lessee covenants to construct buildings, structures, or other capital improvements for industrial or commercial purposes, the cost of which is equal to or greater than 2/3 of the proceeds of disposition.

COMMENT: This change is necessary to provide exemption for leasebacks and other long-term leases where economical value is to be added to the land as a part of the transaction.

Lease valuation: Lease of less than entirety of building:

70. RECOMMENDATION: That the Lieutenant Governor-in-Council make a regulation under Section 23(2)(j) defining the procedure to follow where less than the entirety of a building or property is disposed of by way of lease.

COMMENT: The valuation problems of valuing only a part of a building where the tenant has rights to only certain parts of the building, should be overcome by providing some simple rules. One suggestion is that the relationship of land to buildings on the whole property should govern each lease of a part of the property.

Adjusted Value of Designated Land:
Where lease disposition created taxable value

71. RECOMMENDATION: That the Lieutenant Governor-in-Council make a regulation under the provisions of Section 23(2)(j) defining "adjusted value" for the purposes of a disposition described in Section 1(1)(d)(iii) to include the "taxable value" of any disposition by way of lease in respect of which tax has been paid and any improvements added by the lesses but for greater certainty, should exclude any amount for the value of the lease, unless actually paid by the lessee to the lessor as consideration for entering into the lease.

COMMENT: This regulation would provide some rules to govern the adjusted value of a leashold interest subsequently disposed of and also would prevent the multiple taxation of the same property.

Lease valuation: Proceeds of disposition of lease

72. RECOMMENDATION: That the Lieutenant Governor-in-Council make a regulation under the provisions of Section 23(2)(j) defining proceeds of disposition for the purposes of Section 1(1)(d)(iii) to be

(a) the fair market value of the property immediately after the lease was entered into, or

(b) where the amounts and times of payment of rent under the lease are reasonably determinable, the present value of the lease payments (determined as if the lease payments were computed, or to be computed, on a net-net basis) determined on the basis of a discounting factor that reasonably reflects the then current market interest rates, and the resultant amount is less than the amount in (a).

COMMENT: The most difficult question on leases faced by the Committee was to find an equitable method of determining proceeds of disposition. The present value computations can be done in so many different ways, each of which has some merit, that a simple method must be determined. The valuation of the property itself, taking into account the effect the lease has had on the value of the property, seemed to us to be a method to get around the problem.

/ DEEMED DISPOSITIONS,
/ROLLOVERS, DEDUCTIBILITY

TAX IMPOSED UNDER LSTA ON DESIGNATED LAND OF A CORPORATION AND PAYABLE BY A CORPORATION, WHERE SHARES TO WHICH ARE ATTACHED 50% OR MORE OF THE VOTING RIGHTS ARE TRANSFERRED OR ALLOTTED, IN THE CASE OF A CORPORATION 50% OR MORE OF WHOSE ASSETS CONSIST OF DESIGNATED LAND

The policy of the Government apparently is that the speculation in land intended to be cured by the Act with respect to transfers of land, would be present in the case of a sale of control of a corporation owning designated land. However, in order to devise an administratively practicable scheme, it has been determined that only corporations owning land constituting 50% or more of the assets of the corporation, shall be subject to the 50% land speculation tax in the case of a transfer of voting share control of the corporation. The arbitrariness of selecting the 50% asset test for designated land is obvious, especially when one considers that at any particular date a corporation may be under that percentage and within a week be over that percentage. Suggestions are set forth below to deal with this particular test which is regarded by the Committee as being subject to serious abuse. In this connection, it is to be noted that the test relates to assets only irrespective of the amount of liabilities of the particular corporation.

The Committee has given consideration to the question of whether a tax should be imposed where voting share control of a corporation owning land and meeting the 50% asset test (or whatever other test is to be devised) has been changed. Having regard to the intention of the LSTA to impose a tax on land transfers where economic value of a prescribed amount or of a particular character has not been added to the land by the transferor thereof or where the land is unimproved, the Committee finds some justification for the view that if a change of share control of a corporation owning land were not subject to tax under the Act, the Act could too easily be avoided. Furthermore, since the intention of the Act is to put a halt to escalating land prices by requiring an owner to add economic value thereto, it was considered that a control change at a share price reflecting an increment over the land cost to the corporation under circumstances where the particular corporation has not added any economic value to the land, will result in the price of the land owned by that corporation being increased on an ultimate sale thereof by the corporation. This will be so since the purchaser of the shares will require his corporation to exact a higher price for its land than might

have been exacted by the original owner of the shares of the corporation, to take account of the investment of the purchaser in the shares of the corporation. The Committee understands the Ministry's rationale in imposing the tax at this stage of the change of control notwithstanding that an ultimate disposition of the land by the corporation conceivably would be exempt from tax by reason of the provisions of section 4, section 20 or section 21. A sale of control at the stage before the corporation attains the exemption status set forth in section 4(d) or (g), or before the requisite time period is attained under section 20, or before the subdivision agreement has been complied with under section 21, is comparable to a sale of the land at that particular time by the corporation concerned which does give rise to tax under the Act payable by the corporation.

The chief criticism that has been made by Committee members and others with respect to the imposition of the tax on the sale of control is that a minority shareholder who has not sold his shares concurrently with the change of control will see the value of his investment reduced by virtue of the land speculation tax payable by the corporation. The burden borne by the minority shareholder in this respect is not necessarily alleviated by the corporation being granted a stepped-up basis to the fair market value of the designated land at the particular time, since the disposition ultimately made of the designated land by the corporation may in any event be exempt from tax under one of the exemptions set forth in section 4 or either under section 20 or 21. If an exemption is applicable on an ultimate disposition by the corporation, the result will be that speculation tax will have been paid by the corporation by reason of the change of control and for that reason only, and consequently the minority shareholder will have borne his proportionate burden of the tax precipitated by an event over which he has no control. The burden imposed on the minority shareholder is even more iniquitous when it is considered that the new majority shareholder in effect will not have borne any portion of the tax himself. This latter consequence stems from the fact that the new majority shareholder in negotiating the price of the shares acquired

by him from the old majority shareholder will take cognizance of the land speculation tax to be imposed upon the corporation by virtue of the transaction under the LSTA. In other words, the purchase price of the control block will be an amount that will reflect assets less liabilities of the corporation, including the corporation's liability for speculation tax. Accordingly, the speculation tax once imposed upon the corporation will not financially hurt the new majority shareholder who has reflected the same in the purchase price of his shares.

There is a further element of unfairness in requiring the minority shareholder to effectively bear a portion of the land speculation tax imposed on the corporation where control changes. The purchase price negotiated between the vendor and the purchaser of the controlling block will reflect not only the land speculation tax but also income taxes payable by the corporation in connection with the sale of any of its land or on the winding-up of the corporation, as well as any taxes payable by the shareholder on the winding-up of the corporation. However, the deemed disposition of the land arising on a sale of share control gives rise to proceeds of disposition equal to the fair market value of the land notwithstanding that the price of the shares will reflect an amount less than the fair market value of the land. The Committee recognizes that selecting the fair market value of designated land as the proceeds of disposition is convenient from an administrative point of view, as opposed to endeavouring to deem a proceeds of disposition reflective of the price paid for the shares owned by the controlling shareholder. It is obvious difficulties can arise in determining the appropriate amount to be attributed to a particular parcel of land where the sale price of the shares takes into account not only the assets of the corporation but also its liabilities including as set forth above potential liabilities for income tax and the liability for land speculation tax. One example may demonstrate problems that would arise in attributing proceeds of disposition to designated land based upon the sale price of the controlling shares. A corporation owning an apartment building may have mortgaged it up to its fair market value at

the particular time. Assuming that corporation has additional assets, the purchase price of the controlling shares will in effect take account of the fact that no value should be attributed to the apartment building. Employing this technique therefore gives rise to no tax in respect of the apartment building whereas a sale of that apartment building by the corporation would be based on the fair market value of the parcel irrespective of the mortgage liabilities attached thereto. Notwithstanding the problems created by relating the deemed proceeds of the land to the sale price of the controlling shares, the Committee believes that some correlation should be attempted, and a recommendation with respect thereto is made below.

With a view to relieving the minority shareholder from bearing the burden now imposed upon him by reason of the tax being levied upon the corporation where share control changes, submissions have been made to the Government that the tax imposed on a sale of control be a tax imposed upon the selling shareholder. Such a submission overlooks the constitutional restraints imposed upon the Government of Ontario under the British North America Act, whereunder Ontario is limited to direct taxation within the Province. Such a transfer tax would result in the tax being imposed only upon residents of Ontario. Non-residents of Ontario could not be made subject to the tax unless the transaction took place in Ontario or the situs of the shares was in Ontario. Either of the foregoing two circumstances could be avoided; the first by effecting the transaction outside Ontario and the second by ensuring that there was a register of transfers for effecting the transfers outside of Ontario. It is recognized as well that an Ontario corporation may be continued under the corporation statutes of provinces having complementary legislation to The Business Corporations Act of Ontario, such as the Province of Alberta.

The Committee raises the tentative suggestion after a preliminary study of the question that a suitable mechanism to relieve the minority shareholder from bearing any proportion of the tax payable by the corporation is for the Province to grant a refund to the minority shareholder payable to him only if an eventual sale by the corporation of the designated land would give rise to an exemption. Where the corporation does not sell the designated land but

is in a position that if it were to do so the sale would be an exempt transaction, the minority shareholder should thereupon become entitled to the refund. The Committee believes that the refund mechanism should be applicable not at the stage where the majority shareholder sells control but rather at the aforesaid time of sale by the corporation of its land or the time the corporation is in a position to sell and obtain the exemption. There is no point in making the refund mechanism operative at the earlier time of the sale of control since an ultimate sale of the land by the corporation might not be exempt, in which case the earlier payment of tax simply constitutes a prepayment of the tax.

For the purpose of administrative simplicity, it is suggested that the refund be payable to a minority shareholder only where he held his shares at the time of the deemed disposition which gave rise to the initial land speculation tax payable by the corporation. It can be recognized that a minority shareholder who disposes of his shares subsequent to the date of a deemed disposition has himself, to some extent, speculated in his shares and consequently there is no injustice by not making the refund payable to him.

The Committee believes that a refund mechanism of the nature above described can be workable only if there is cooperation between the Ontario Government and the Federal Government. For example, any characterization of the refund payment made to the minority shareholder would be subject to interpretation of the federal taxation authorities for purposes of the Income Tax Act (Canada) and ultimately by the Courts. To avoid the confusion that is now present between the two governments with respect to the deductibility of the speculation tax for income tax purposes, it will be necessary for there to be an amendment to the Federal Income Tax Act to stipulate the consequence to the minority shareholder stemming from the payment to him of a refund by the Ontario Government.

The suggestions of the Committee set forth below do not deal further with the minority shareholder problem but it is our belief that the problem should be explored in depth by the Government. The suggestions do,

however, take into account the loopholes existing in the present provisions especially as they relate to the deemed disposition arising as a result of the transfer of shares or the allotment of shares in a corporation.

Because of the limited time available to the Committee, the corporation problems arising from the deemed disposition rules of the LSTA are set forth in the form of observations and tentative suggestions as opposed to recommendations, in the hope that discussions will thereupon be initiated within the Ministry.

I. Deemed dispositions - transfer or allotment of shares of a corporation:

OBSERVATION:

(A) As presently worded, the deemed disposition rule contained in clause (d)(vi) applies where shares carrying 50% or more of the voting rights attaching to all shares of the corporation are transferred or allotted. Consider, however, the situation where shares constituting at least 50% of the equity shares of a corporation otherwise meeting the asset test, (being shares that participate in the growth of a corporation as opposed to non-equity shares which are entitled to a fixed rate of return and do not participate in the growth of a corporation) but not carrying 50% of the voting rights attaching to all shares, are transferred or allotted. There are circumstances where a purchaser of shares may be content to acquire the equity shares in a corporation without concurrently acquiring 50% of the votes exercisable at meetings of shareholders. Such purchaser may be content to have voting control of the corporation continue to lie with another party who is amicably disposed to him.

The present language of the definition affords the opportunity to structure a transaction in such a manner as to avoid a disposition from occurring. For example, if a sole shareholder of a corporation owns 100 common shares representing all of the issued and outstanding shares, he can cause the corporation to issue to him 99 voting redeemable preference shares of a nominal par value and thereafter convert the 100 common shares into non-voting common shares. Upon the sale of the 100 common shares to a purchaser, sub-clause (d)(vi) will not be applicable. Subsequent to this sale, the common shares can be made voting again and the redeemable preference shares redeemed. Section 6, the anti-avoidance section of the LSTA, will not apply since that section requires that designated land be disposed of, whereas the effect of the foregoing transactions is to preclude a disposition of designated land from arising.

The suggestion hereunder will result in a deemed disposition arising on the transfer or allotment of 50% of the equity shares in the capital of the corporation.

SUGGESTION:

(A) The transfer or allotment requirement for corporations meeting the 50% asset test be in respect of a transfer or allotment of either

(i) shares carrying 50% or more of the voting rights attaching to all shares, OR

(ii) participating shares representing in the aggregate 50% of more of all the participating shares of the corporation, where "participating share" is defined in a similar manner to the definition of "equity share" under paragraph 257(2)(e) of the Income Tax Act for purposes of determining whether a corporation has a degree of Canadian ownership.

OBSERVATION:

(B) An amendment is required to clarify the ambiguous expression "50 per cent or more of the assets", which gives rise to problems of interpretation as to whether the intention is to count assets of a corporation by number, use a book value basis in respect of the assets of the corporation, or use a fair market value basis for such assets. The most logical treatment is the selection of a fair market value of its assets consisting of designated land, prior to a transfer of shares, bonds, bank notes or other types of investments, including cash thereby avoiding the applicability of the 50% rule. To avoid such "stuffing of assets" taking place prior to an effective sale of control, it is suggested that the deemed disposition rule apply to a corporation which has satisfied the 50% asset test throughout a 30-day period included in the six-month period ending at the time of the transfer of the shares. It is believed that the use of a 30-day period will ensure that a corporation will not inadvertently meet the 50% test at one point in time by reason of some event unrelated to the value of its real estate (such as a decline in the stock market reducing the value of its other investments), and shortly thereafter return to its normal status of not satisfying the 50% asset test.

SUGGESTION:

(B) The expression "50 per cent or more of the assets of which consist of designated land" be amended to "at least half the fair market value of the assets of which throughout any 30-day period included in the period commencing six months before the share transfer or allotment and ending on the date thereof, consisted of designated land".

OBSERVATION:

(C) As presently worded, the definition of disposition applies on the requisite number of shares being transferred or allotted via a single transfer or allotment. It is suggested that a disposition should arise where the requisite number of shares is transferred or allotted by means of a series of transfers or allotments as opposed to a single such transfer or allotment, for the purpose of avoiding the application of the definition.

The Committee recognizes the problems generated when tax is made exigible upon an anti-avoidance purpose being ascertained, but believes that an expansion of the definition to cover the foregoing situation is necessary. Again, Section 6 of the LSTA would not be applicable since it is a condition of its application that a disposition has occurred, whereas the consequences of the action taken by the series of transactions is to preclude a disposition from arising.

SUGGESTION:

(C) Where a number of shares of a corporation have been transferred or allotted in a series of transactions such that if the said number of shares had been transferred or allotted in a single transaction, the definition of "disposition" would be applicable, and one of the main purposes of the transfer or allotment of the said number of shares having been effected in a series of transactions as opposed to one transaction, was to avoid the applicability of the definition of "disposition" as set forth in sub-clause (vi) of clause (d), the said definition shall be applicable.

OBSERVATION:

(D) As presently worded, a disposition will arise if the controlling shareholder owning shares carrying more than 50% of the votes attached to all shares of the corporation, has allotted and issued to him by the

corporation shares carrying more than 50% of the votes exercisable at shareholders' meetings notwithstanding that there has not been a change of control.

An amendment is suggested to ensure that an allotment and issue of shares can only give rise to a disposition where a change of control is thereby effected.

SUGGESTION:

(D) The definition shall not include an allotment and issue of shares that does not give rise to a change of control of a corporation.

II. Deemed dispositions - chain corporation concept:

OBSERVATION: The definition of "disposition" contained in Section 1(1)(d)(vi) extends only to a transfer or allotment of shares of a corporation owning land. However, a sale of shares of a corporation not satisfying the 50% asset test but controlling the land corporation that does satisfy the asset test, will not be subject to the LSTA, notwithstanding that in substance the aforesaid transaction may be equivalent to the sale of the shares of the land corporation. The corporation owning the shares (hereinafter called the "holding corporation") may have acquired the shares of the land corporation by means of one of the following methods:

(i) an acquisition of the shares at a time when the land corporation did not satisfy the 50% test;

(ii) an acquisition of the shares at a time when the land corporation did satisfy the 50% test but the proceeds of disposition did not exceed the adjusted value of the land owned by the land corporation;

(iii) an acquisition that was the subject matter of a roll-over exemption, the shares having been acquired for example from the controlling shareholders of the holding corporation.

NOTE: This (iii) assumes a rollover exemption in respect not only of a transfer of land into a corporation controlled by the transferor, but as well in respect of a transfer of shares of a corporation meeting the 50% asset test.

(iv) an acquisition at a time before April 9, 1974.

On the transfer of the requisite number of shares of the holding corporation, query whether there is any reason why a disposition of the designated land owned by the land corporation should not occur. None of the four modes of acquisition outlined above give rise to any equities militating against a deemed disposition of designated land owned by the land corporation. If the premise is accepted that a sale of the requisite number of shares of a corporation satisfying the 50% asset test should result in a deemed disposition of the land of such corporation, then it appears that a two-tier corporate structure (whether arising at the inception of the two corporations or by virtue of a later acquisition of one corporation by another) ought not to be available as a device to avoid the impact of the tax.

The two-tier corporate set-up as a possible device to avoid a deemed disposition on a sale of shares constitutes the simplest example of the problems posed by the existence of a tier of corporations. This problem has been dealt with for designated surplus purposes in the Income Tax Act (Canada) by means of a chain corporation concept. In the limited time at its disposal, the Committee has not been able to even consider the application of that concept to the LSTA, but further consideration might be given to this area.

One of the difficulties stems from the fact that as in the case of two-tier corporate structures, the existence of a tier of at least three corporations may originate for purposes totally extraneous to income tax considerations or tax considerations under the LSTA. Should a sale of shares of a top corporation create a deemed disposition of land owned by the third or fourth corporation down? In this context of a controlled group of more than two corporations, the Committee puts forth the suggestion below dealing only with a two-tier corporate set-up.

The Committee at this stage does not suggest the inclusion in the LSTA of an anti-avoidance provision similar to subsection 247(1) of the Income Tax Act (Canada) to deal with this problem of tier corporations for the simple reason that specific rules are always preferable to general rules depending upon an intention that is often difficult to fathom.

SUGGESTION: That an amendment be made so as to define a disposition of designated land owned by a corporation satisfying the 50% asset test (hereinafter called the "land corporation") as arising upon the sale or transfer in any manner of the beneficial interest in or the allotment and issue of, the requisite number of shares of a second corporation not satisfying the 50% asset test and owning the requisite number of shares of the land corporation.

III. Deemed disposition - rollover to corporation followed by transfer of shares:

OBSERVATION: Assume that the LSTA provides for a Section 85 Income Tax Act (Canada) (Section 79 of the Ontario Corporations Tax Act) rollover exemption and that the same has been taken under the LSTA in either of the two following situations:

(i) a transfer of shares of a corporation (the "land corporation") satisfying the 50% test to another corporation controlled by the transferor;

(ii) a disposition of designated land by a transferor to a corporation controlled by the transferor.

In situation (i), assume a subsequent sale of the requisite number of shares of a corporation that controls the land corporation via intermediate share holdings in circumstances where our Suggestion on II Deemed dispositions - chain corporation concept is not applicable because the controlling corporation does not itself own the requisite number of shares of the land corporation. It is suggested this subsequent sale should give rise to a deemed disposition of all the designated land of the land corporation provided that the latter still satisfies the 50% asset test. It is believed that this rule should apply whether or not the controlling corporation itself satisfies the 50% asset test.

In situation (ii), assume a subsequent sale of the requisite number of shares of a corporation that controls the land corporation, irrespective of whether or not the land corporation at such time satisfies the 50% asset test. It is suggested this subsequent sale should give rise to a deemed disposition of that designated land owned by the land corporation which previously was the subject matter of the Section 85 type rollover.

Query whether a rollover exemption taken in respect of a transfer of shares of the controlling corporation should result in the deemed disposition rules suggested herein not applying. It is likely that a deemed disposition should not occur in the land corporation where an exemption is granted in respect of the transfer of shares of a corporation controlling the land corporation.

It should be noted that a controlling corporation for these purposes, as in the case of the associated corporation legislation contained in the Income Tax Act (Canada) and the case law interpreting the same, would be either the top tier corporation in a chain of corporations or a corporation beneath the top tier corporation, but higher in the chain than the land corporation.

SUGGESTION: That where a rollover exemption has been availed of under the LSTA in respect of a transfer of shares or a disposition of land to a corporation controlled by the person making the transfer or disposition, a subsequent sale or transfer of the beneficial interest in, or the allotment and issue of, the requisite number of shares of a corporation controlling directly or indirectly the corporation whose shares were so transferred or controlling directly or indirectly the corporation to whom the designated land was so disposed, as the case may be, shall result in a deemed disposition of all the designated land owned by the corporation whose shares were so transferred if such corporation satisfies the 50% asset test, and a deemed disposition of that designated land so disposed of to the transferee corporation irrespective of whether or not such transferee corporation at the relevant time satisfies the 50% asset test.

IV. Value of designated land on deemed disposition:

OBSERVATION: As set forth in the prefatory remarks to this discussion relating to the deemed disposition of designated land arising on a transfer or allotment of the requisite number of shares of a corporation, it may be unfair that the proceeds of disposition of such designated land should be equal to the fair market value thereof. The unfairness lies in the fact that the price of the shares inevitably reflects an amount less than the fair market value of the designated land since it takes into account potential liabilities for income tax and land speculation tax exigible under the LSTA.

The Committee recognizes the impossibility of the legislation setting out a formula whereby the proceeds of disposition of the designated land can be tied directly to the sale price of the shares. However, with a view to affording some relief to the corporation which bears the tax, it is suggested that an amount less than fair market value of the designated land be deemed the proceeds of disposition where it can reasonably be considered that the purchase price of the shares was reduced to take into account the factors outlined below.

> SUGGESTION: That Section 1(9) of the LSTA be amended to provide that where a transfer or allotment of shares gives rise to a deemed disposition under sub-clause (vi) of clause (d), of designated land of a corporation, the proceeds of disposition of the designated land shall be the fair market value of the designated land at the time of the deemed disposition, less an amount that can be reasonably considered as having been discounted on the purchase of the shares by reason of the factors likely taken into account in establishing the said sale price of the shares transferred or allotted, including the corporation's potential liability for income tax arising on the sale of any designated land and the corporation's potential liability for tax under the LSTA.

V. Deemed disposition - amalgamation:

OBSERVATION: It is suggested that sub-clause (d)(vii) need extend only to statutory corporate mergers to protect the Revenue from leakage, and only in those cases where the merging corporation satisfying the 50% asset test is controlled otherwise than by the person or group of persons controlling the corporate entity resulting from the amalgamation. Where there is not a change of control there is no real change of economic interest justifying the imposition of a tax, either under Section 2(1) ("the speculative tax") or under Section 2(2) ("the land transfer tax"). The type of amalgamation contemplated is that described in Section 196 of the Business Corporations Act (Ontario) and in Section 137 of the Canada Corporations Act. Section 87 of the Income Tax Act (Canada) and Section 81 of the Ontario Corporations Tax Act as well deal with this type of amalgamation. The statutory mergers contemplated herein however also entend to foreign statutory mergers.

If amalgamations did not give rise to a deemed disposition, the way would be open for large corporations to merge with smaller corporations having land sought by the former corporations, and thereafter shareholders who held shares previously in the larger corporation could acquire the shares of the amalgamated entity held by the previous shareholders of the small corporation without attracting the provisions of the deemed disposition rules contained in the Act. However, rollover exemptions are suggested elsewhere in respect of amalgamations of public corporations. The expression "merger, consolidation or any other like arrangement" now found in sub-clause (vii) is ambiguous and not required to protect the Revenue against leakage, since an ordinary disposition of land will inevitably result on any other form of consolidation other than a statutory merger.

SUGGESTION:

(A) That sub-clause (vii) of clause (d) of Section 1(1) be repealed and there be substituted in lieu thereof a provision of the following effect - The amalgamation by means of a statutory merger of two or more corporations, where at least half the fair market value of the assets of one or more of the said corporations throughout any 30 day period included in the six-month period commencing six months before amalgamation and ending on the date thereof consisted of designated land (which corporation is herein called the "designated land corporation") to form

one corporate entity, where the designated land corporation was immediately before the amalgamation controlled by a person or group of persons different from the person or group of persons that controlled the corporate entity resulting from the amalgamation immediately thereafter.

(B) That any amalgamation by statutory merger of two or more corporations not resulting in a disposition as set forth in (A) above, shall give rise to rollover treatment in respect of any designated land held by a merging corporation.

VI. Control - Definition in Section 1(5):

OBSERVATION: The present definition of control of a corporation is imperfectly worded. A "control test" is required for purposes only of sub-clause (vii) of clause (d) and for the purpose of Section 2(2). The suggested definition below is adopted from the language contained in the pre-1972 Income Tax Act relating to a personal corporation.

> SUGGESTION: That Section 1(5) be repealed and in lieu thereof a provision of the following effect be substituted. For the purpose of the LSTA, "control" of a corporation means control whether through holding a majority of the shares of a corporation or in any other manner whatsoever, and the word "controlled" has a comparable meaning.

VII. Section 2(2) - Sale of less than 100% of the shares of a corporation:

OBSERVATION: Section 2(2) as presently drafted is predicated upon a 20% tax being payable on the fair market value of the designated land owned by a corporation satisfying the 50% test, where the result of the transfer or allotment of the requisite number of shares is that control of the corporation has changed and the corporation is immediately after such transfer or allotment a non-resident corporation as defined in the Land Transfer Tax Act, 1974. This rule imposes the 20% tax on a 100% interest in the designated land notwithstanding that non-residents have not acquired 100% of the outstanding shares of the corporation, and for that matter may only have acquired 50% of the shares of the corporation.

Inequitable consequences flow from the foregoing principle. Assume that A, a Canadian, and B, a non-resident, acquire ownership of 100% of the outstanding shares of a corporation meeting the 50% asset test, the shares being divided equally between them. A deemed disposition occurs under sub-clause (vi) of clause (d) and the combined effect of Section 1(9) and Section 2(2) of the LSTA is that a 20% tax is imposed on the fair market value of the designated land, notwithstanding that B does not himself have control over the corporation but in fact only owns 50% of the outstanding shares. Assume that subsequently B decides to acquire the 50% of the shares held by A. Section 2(2) is again applicable since control of the corporation is now exercisable by a person different from those by whom control was previously exercisable. Again the 20% tax is imposed on the fair market value of 100% of the designated land. This is certainly an inequitable result.

Since the deemed disposition test arises on a transfer or allotment of 50% of the shares of a class (whether voting or participating shares as suggested in our SUGGESTION I), it is suggested that where a shareholder whose previous acquisition of shares gave rise to the payment of tax under Section 2(2), acquires more shares of the corporation causing a change of control, the corporation ought not to pay the full tax. The tax otherwise payable should be reduced by the proportion thereof, that the shareholder's holding of shares at the time of the prior payment of tax bore to the number of shares

of the corporation that constituted 50% of the outstanding shares of the particular class. In the example provided above, where B on the previous acquisition acquired 50% of the shares of the corporation, the tax otherwise payable on the acquisition of the remaining 50% from A is eliminated since the tax otherwise payable is reduced by the proportion of in effect 50/50.

Another example will illustrate the manner in which this suggestion could operate where a number of shareholders constitute a group that has acquired control. Assume that all of the shares of the corporation are acquired by A, B, and C who are Canadians holding 50% of the outstanding shares and D, E, and F, who are non-residents holding the remaining 50% of the shares in equal amounts. The tax is of course exigible under Section 2(2) since 50% of the shares are transferred to non-residents. Subsequently, E and F determine to acquire all of the shares held by A, B, C, and D, representing 66 2/3% of the outstanding shares.

As presently drafted the full tax is again exigible. The effect of the suggestion is that the tax otherwise payable is reduced by the fraction of $\frac{33\ 1/3}{50}$ or 2/3. In other words, 1/3 of the tax becomes exigible, a result that is equitable and in accordance with the substance of the transaction whereby E and F acquired a further 1/3 of the outstanding shares of the corporation in order to bring them up to the 50% level.

The suggestion has been made that the tax payable under Section 2(2) be related to the percentage of shares of the corporation that is changing hands, in order to equate an acquisition of shares to a direct acquisition of land by the non-resident. Yet, proponents of this view do not advocate that the tax be exigible where less than 50% of the shares are transferred or allotted as in the case of direct ownership of land. To accede to such proposal would result in further inconsistencies.

It has also been suggested that a transitional rule be adopted in respect of a corporation whose shares were held on April 9, 1974 to an extent not exceeding 50% by non-residents, to provide that where some or all of such

non-residents subsequent to such date acquired a further 50% of the shares of the corporation the tax should be imposed on the fair market value of a 1/2 interest in the designated land instead of being imposed in respect of a 100% interest in the designated land. Advocates of such a suggestion point out that if the non-residents held their interests in the land on April 9, 1974 directly as opposed to indirectly via the corporation, any subsequent increase in their interest in the land would produce tax under The Land Transfer Tax Act, 1974 in respect of the additional interest acquired as opposed to in respect of 100% of the designated land. Such observation is of course correct but it must be borne in mind as well however that Section 2(2) of the LSTA is operative only where 50% of the shares of the corporation are allotted or transferred, while the Land Transfer Tax Act, 1974 is operative in respect of the acquisition of any percentage interest in the land. Accordingly, those proposing this change are in effect endeavouring to obtain the best of both worlds. Notwithstanding the foregoing remarks the Ministry may wish to provide a transitional rule to cover the position where non-residents held not more than the requisite shares on April 9, 1974 in a corporating meeting the 50% test.

SUGGESTION: That Section 2(2) of the LSTA be amended to add thereto a proviso to the effect that on a disposition occurring by reason of the events described in sub-clause (vi) of clause (d) where the transfer or allotment of the requisite number of shares of the corporation is to a person or group of persons in respect of whose prior acquisition of shares in the corporation a tax was exigible under the said Section 2(2), the tax otherwise payable shall be reduced by a fraction whose numerator is the number of shares owned by such person or group of persons immediately after the disposition that gave rise to the said tax on the prior acquisition, and whose denominator is the number of shares of the class that constituted 50% of the shares of the class owned by the person or by the group, as the case may be, immediately after the said disposition that gave rise to the said tax on such prior acquisition.

LAND SPECULATION TAX ACT, 1974

ROLLOVERS

A "rollover" is a mechanism whereby assets are transferred among related parties without any actual or deemed realization and therefore without any immediate tax cost. The tax impact of such transfers is deferred until such time as the transferee disposes of the assets (or is deemed to have disposed of the assets) to an arm's length party, normally through carrying over the "cost basis" of the property to the new non-arm's length owner. In essence, a rollover is a means of deferring the payment of tax that would otherwise arise on a transfer which does not involve a substantial shift in economic ownership, until the time when such a change in "real" ownership does occur.

The Committee is firmly of the view that the Land Speculation Tax Act (and also the Land Transfer Tax Act) should be amended to provide for such a deferral of tax. Failure to provide an exemption where land has been transferred between related parties will unfairly penalize many transfers arranged in common business reorganizations, and unduly inhibit the flexibility of Ontario land owners to rearrange their affairs for reasons unconnected with tax avoidance.

Generally speaking, rollovers similar to those contained in the federal Income Tax Act and the Ontario Corporations Tax Act should also pertain in the case of the Land Speculation Tax Act. Such rollovers should include a deferral of tax in all of the following transfers:

- interspousal transfers
- intra-family transfers
- transfers on death (at fair market value)
- principal residence to testamentary trust
- amalgamations
- winding-up of wholly-owned subsidiary
- incorporation of proprietorship
- incorporation of partnership
- transfer to partnership
- winding-up of partnership
- sale to an 80%-owned subsidiary

Our specific tentative recommendations on certain of the above proposals are as follows:

1. We recommend that a further exemption be added to Section 4 of the Land Speculation Tax Act to provide that no tax is payable when designated land is transferred from one spouse to another.

Interspousal transfers of property have already been widely recognized as transactions which should not give rise to tax. This is reflected in the Income Tax Act (Canada), the Ontario Corporations Tax Act and the Ontario Gift Tax Act. There would appear to be no reason for imposing a tax on an interspousal transfer (whether by sale or gift) under the Land Speculation Tax Act, although the "cost basis" of the land to the transferring spouse should become the initial cost basis to the spouse receiving the property.

2. Where designated land is disposed of to a member of the family as defined in Section 1(1)(g), we recommend that no tax should be payable at such time but that the adjusted value of the transferor at the time of disposition should be the deemed adjusted value of the transferee.

3. We recommend that a provision be added in Section 4 to clarify that if the transferor is the beneficiary of the designated land under a last will and testament or on the intestacy of any person, and that person would have been entitled to an exemption under Section 4, the transferor would be entitled to the exemption to which that person would have been entitled to had he been the transferor.

4. We recommend that the exemptions listed in Section 4 be expanded to provide for tax exempt rollovers of designated land in the situations described below:

(a) Rollover from an individual to a corporation controlled by the transferor immediately after the transfer.

Section 85(1) of the Income Tax Act (Canada) provides for a rollover from an individual owning 80% of the shares of a corporation to that corporation. (It is proposed under the recent federal Budget that this exemption be broadened to provide a rollover in virtually all transfers of assets to a company for shares.) A similar rollover exists under Section 85(2) of this Act in the case of transfer from a

partnership to a corporation, 80% of whose shares are owned by the partnership. This exemption is obviously justified because of the limited effective change of control which occurs in these circumstances with respect to the transferred property, and we would suggest that it be included in the Land Speculation Tax Act.

(b) Rollover from trust to beneficiary.

Section 107(2) of the Income Tax Act (Canada) provides for a rollover of property out of a trust to a resident beneficiary, and in certain circumstances to a non-resident beneficiary. The Land Speculation Tax Act only provides for such a rollover in circumstances where no "disposition" occurs because there is a change in the legal ownership of the property without any change in the beneficial ownership thereof (Section 1(1)(b)). In the case of the vast majority of trusts, a beneficiary does not have any beneficial ownership in the underlying assets and therefore the disposition of designated land from such a trust will give rise to the imposition of Land Speculation Tax unless a particular exemption in Section 4 is available.

(c) Other rollovers.

The Ontario Income Tax Act, Ontario Corporations Tax Act and the Income Tax Act (Canada) provide for extensive rollovers. The Land Speculation Tax Act provides for only one rollover - the transfer of land on the winding-up of a corporation and the distribution of its assets to its shareholders when at least 50% of the assets of the corporation consist of designated land.

We recommend that the following further rollovers be considered, with appropriate safeguards to prevent revenue leakage:

Relevant provisions		
Federal Income Tax Act	Ontario Corporations Tax Act	Type of Transfer
85(1)	79(1)	Transfer of property to corporation by controlling shareholder
85(2)	79(2)	Transfer of property to corporation from partnership
85(3)	79(3)	Transfer of property on winding-up of partnership
86	80	Reorganization of capital of corporation (for deemed dispositions)
87	81	Statutory amalgamation (deemed disposition)

Relevant provisions

Federal Income Tax Act	Ontario Corporations Tax Act	Type of Transfer
88	82	Winding-up of subsidiary (regardless of assets)
97(2)	86(2)	Contribution of property to partnership
107(2)	96(2)	Disposition by trust in satisfaction of capital interest
98(3)	87(4)	Transfers where partnership ceases to exist

We further recommend that where a principal residence is disposed of to a trust in favour of a spouse the "character" of the principal residence should flow through to the trust. (See Subsections 40(4) and 40(5) of The Income Tax Act (Canada).)

The Committee, in the limited time at its disposal, has not had a full opportunity to consider all of the details necessary to implement its suggestions for a substantial expansion of the "rollover" provisions of the new legislation. However, the Committee urges that an immediate start be made on the appropriate revisions to the Acts and regulations to implement the highly desirable objective of removing impediments to transfers arising out of commercial and business reorganizations.

Commentary on deductibility of land speculation tax for income tax purposes:

In the event that the tax imposed by the LSTA is considered not to be a deductible expense for federal income tax purposes, we suggest that consideration be given to amending the definition of "net costs of disposition" to include any income taxes otherwise payable under Section 123 of the Income Tax Act (Canada) as a result of the disposition of designated land in Ontario. As a further alternative, the Minister might propose lowering the rate of land speculation tax to 25%.

In his Budget speech of April 9, 1974, the Treasurer of Ontario has made it clear that the LSTA is not to be considered as a revenue-raising statute. In fact, it would appear from a reading of the Budget speech that if no tax is collected the policy objectives of the statute will have been achieved. The attached schedule indicates that the same effective rate of tax can be achieved if any income taxes in respect of the sale of designated land are treated as a deduction in computing the taxable value for purposes of the LSTA. Although the effective rate is maintained, there is a shift in the allocation of revenue from the Provincial to the Federal government.

While the total income tax and land speculation tax borne by the taxpayer would be the same amount in the aggregate whether the land speculation tax were treated as deductible expense or the income tax liability were included in "net costs of disposition", the latter solution adversely affects the cumulative deduction account of those persons disposing of designated land which are Canadian-controlled private corporations.

An alternative solution is to lower the rate to 25%, however, this would continue to adversely affect the cumulative deduction account of a Canadian controlled private corporation, but to a lesser extent.

ANALYSIS OF TAX EXIGIBLE:

Assumptions (a) the gain subject to tax forms part of "active business income" of the corporation

(b) the individual has a marginal tax rate of 30%

(c) the gain amounts to $200

(d) the corporate tax rates are 1974 rates as defined in Section 123 of the Income Tax Act (Canada)

If land speculation tax is not deductible -

	Individual	Public/other private corporation	Canadian controlled private corporation
Gain on sale of land	$200	$200	$200
Income taxes thereon	60	100	54
	$140	$100	$146
Land speculation tax	$ 70	$ 50	$ 73
Total taxes	$130	$150	$127

If land speculation tax is deductible -

Gain on sale of land	$200	$200	$200
Land speculation tax thereon	100	100	100
Taxable income	$100	$100	$100
Income taxes	$ 30	$ 50	$ 27
Total taxes	$130	$150	$127

Effect on Cumulative Deduction Account:

From the preceding analysis of tax exigible it can be seen that the Canadian controlled private corporation has $73 available for dividends (being the difference between the $200 gain and $127 total taxes).

The cumulative deduction account is increased by the taxable income and decreased by 4/3 of the taxable dividends paid. If all of the after-tax income is paid out as a dividend the effect on the cumulative deduction account will be as follows:

(a) Assuming speculation tax not deductible:

Taxable income	$200
Deduct: 4/3 of taxable dividends (4/3 x $73)	97
Permanent erosion of CDA	$103

(b) Assuming speculation tax deductible:

Taxable income	$100
Deduct: 4/3 of taxable dividends (4/3 x $73)	97
Effect on CDA due to rounding	$ 3